

MEXICAN ECONOMIC DEVELOPMENT INC

Form 20-F

June 28, 2007

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As filed with the Securities and Exchange Commission on June 28, 2007

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 20-F**

**ANNUAL REPORT PURSUANT TO SECTION 13**

**OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the fiscal year ended December 31, 2006**

**Commission file number 1-14814**

**Fomento Económico Mexicano, S.A.B. de C.V.**

(Exact Name of Registrant as Specified in Its Charter)

**Mexican Economic Development, Inc.**

(Translation of Registrant's Name into English)

**United Mexican States**

(Jurisdiction of Incorporation or Organization)

**General Anaya No. 601 Pte.**

**Colonia Bella Vista**

**Monterrey, NL 64410 Mexico**

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(Address of Principal Executive Offices)

**Securities registered or to be registered pursuant to Section 12(b) of the Act:**

<b>Title of Each Class</b>	<b>Name of Each Exchange on Which Registered</b>
American Depositary Shares, each representing 10 BD Units, each consisting of one Series B Share, two Series D-B Shares and two Series D-L Shares, without par value	New York Stock Exchange

**Securities registered or to be registered pursuant to Section 12(g) of the Act:**

None

**Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:**

None

**The number of outstanding shares of each of the issuer's classes of capital or common stock as of December 31, 2006 was:**

720,392,590 BD Units, each consisting of one Series B Share, two Series D-B Shares and two Series D-L Shares, without par value. The BD Units represent a total of 720,392,590 Series B Shares, 1,440,785,180 Series D-B Shares and 1,440,785,180 Series D-L Shares.

472,349,500 B Units, each consisting of five Series B Shares without par value. The B Units represent a total of 2,361,747,500 Series B Shares.

**Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.**

Yes  No

**If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.**

Yes  No

**Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.**

Yes  No

**Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):**

Large Accelerated filer  Accelerated filer  Non-accelerated filer

**Indicate by check mark which financial statement item the registrant has elected to follow.**

Item 17  Item 18

**Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).**

Yes  No



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**INTRODUCTION**

**References**

The terms FEMSA, our company, we, us and our, are used in this annual report to refer to Fomento Económico Mexicano, S.A.B. de C.V. a except where the context otherwise requires, its subsidiaries on a consolidated basis. We refer to our subsidiary Coca-Cola FEMSA, S.A.B. de C.V., as Coca-Cola FEMSA, our subsidiary FEMSA Cerveza, S.A. de C.V., as FEMSA Cerveza, and our subsidiary FEMSA Comercio, S.A. de C.V., as FEMSA Comercio.

The term S.A.B. stands for *Sociedad Anónima Bursátil*, which is the term used in Mexico to refer to a publicly traded company under the new Mexican Securities Law issued in 2006. In December 2006, both we and Coca-Cola FEMSA changed our name to include the denomination S.A.B. in accordance with the new Mexican Securities Law.

References to U.S. dollars, US\$, dollars or \$ are to the lawful currency of the United States of America. References to Mexican pesos, peso or Ps. are to the lawful currency of the United Mexican States, or Mexico.

**Currency Translations and Estimates**

This annual report contains translations of certain Mexican peso amounts into U.S. dollars at specified rates solely for the convenience of the reader. These translations should not be construed as representations that the Mexican peso amounts actually represent such U.S. dollar amounts or could be converted into U.S. dollars at the rate indicated. Unless otherwise indicated, such U.S. dollar amounts have been translated from Mexican pesos at an exchange rate of Ps. 10.7995 to US\$ 1.00, the noon buying rate for Mexican pesos on December 31, 2006 as published by the Federal Reserve Bank of New York. On June 15, 2007, this exchange rate was Ps. 10.8100 to US\$ 1.00. See Item 3. Key Information Exchange Rate Information for information regarding exchange rates since January 1, 2002. In our previous public disclosures, we presented U.S. dollar amounts based on the exchange rate quoted by dealers to FEMSA for the settlement of obligations in foreign currencies at the end of the applicable period.

To the extent estimates are contained in this annual report, we believe that such estimates, which are based on internal data, are reliable. Amounts in this annual report are rounded, and the totals may therefore not precisely equal the sum of the numbers presented.

Per capita growth rates and population data have been computed based upon statistics prepared by the *Instituto Nacional de Estadística, Geografía e Informática* of Mexico (the National Institute of Statistics, Geography and Information, which we refer to as the Mexican Institute of Statistics), the *Instituto Brasileiro de Geografia e Estadística* (the Brazilian Institute of Statistics or IBGE), the Federal Reserve Bank of New York, *Banco de México* (the Bank of Mexico) and upon our estimates.

**Forward-Looking Information**

This annual report contains words, such as believe, expect and anticipate and similar expressions that identify forward-looking statements. Use of these words reflects our views about future events and financial performance. Actual results could differ materially from those projected in these forward-looking statements as a result of various factors that may be beyond our control, including but not limited to effects on our company from changes in our relationship with or among our affiliated companies, movements in the prices of raw materials, competition, significant developments in Mexico or international economic or political conditions or changes in our regulatory environment. Accordingly, we caution readers not to place undue reliance on these forward-looking statements. In any event, these statements speak only as of their respective dates, and we undertake no obligation to update or revise any of them, whether as a result of new information, future events or otherwise.

**Table of Contents****ITEMS 1-2. NOT APPLICABLE****ITEM 3. KEY INFORMATION****Selected Consolidated Financial Data**

This annual report includes, under Item 18, our audited consolidated balance sheets as of December 31, 2006 and 2005 and the related consolidated income statements, changes in financial position and changes in stockholders' equity for the years ended December 31, 2006, 2005 and 2004. Our audited consolidated financial statements are prepared in accordance with Mexican Financial Reporting Standards (*Normas de Información Financiera*), which differ in certain significant respects from accounting principles generally accepted in the United States, or U.S. GAAP.

Notes 27 and 28 to our audited consolidated financial statements provide a description of the principal differences between Mexican Financial Reporting Standards and U.S. GAAP as they relate to our company, together with a reconciliation to U.S. GAAP of net income and stockholders' equity as well as U.S. GAAP consolidated balance sheets, income statements, cash flows and changes in stockholders' equity for the same periods presented for Mexican Financial Reporting Standards purposes. In the reconciliation to U.S. GAAP, we present our subsidiary Coca-Cola FEMSA, which is a consolidated subsidiary for purposes of Mexican Financial Reporting Standards, under the equity method for U.S. GAAP purposes, due to the substantive participating rights of The Coca-Cola Company as a minority shareholder in Coca-Cola FEMSA.

The effects of inflation accounting under Mexican Financial Reporting Standards have not been reversed in the reconciliation to U.S. GAAP. See note 27 to our audited consolidated financial statements.

The following table presents selected financial information of our company. This information should be read in conjunction with, and is qualified in its entirety by, our audited consolidated financial statements and the notes to those statements. The selected financial information is presented on a consolidated basis and is not necessarily indicative of our financial position or results of operations at or for any future date or period.

**Selected Consolidated Financial Information**

	Year Ended December 31,					
	2006 <sup>(1)</sup>	2006	2005	2004	2003 <sup>(2)</sup>	2002
	(In millions of U.S. dollars and millions of Mexican pesos at December 31, 2006, except for per share data, the weighted average number of shares outstanding and percentages)					
<b>Income Statement Data:</b>						
<b>Mexican FRS:</b>						
Total revenues	\$ 11,707	Ps. 126,427	Ps. 111,636	Ps. 102,316	Ps. 86,818	Ps. 62,542
Income from operations	1,610	17,390	16,403	14,964	13,686	10,973
Taxes <sup>(3)</sup>	445	4,806	4,866	2,649	3,963	4,255
Consolidated net income	851	9,195	8,566	10,085	5,340	5,417
Net majority income	613	6,622	5,766	6,411	3,631	3,332
Net minority income	238	2,573	2,800	3,674	1,709	2,085
Net majority income: <sup>(4)</sup>						
Per Series B Share	0.09	0.99	0.90	1.08	0.61	0.56
Per Series D Share	0.12	1.24	1.13	1.35	0.76	0.70
Weighted average number of shares outstanding (in millions):						
Series B Shares	3,082.1	3,082.1	2,944.9	2,739.2	2,739.2	2,739.2
Series D Shares	2,881.6	2,881.6	2,753.4	2,561.0	2,561.0	2,561.0
<b>Allocation of earnings:</b>						
Series B Shares	46.11%	46.11%	46.11%	46.11%	46.11%	46.11%
Series D Shares	53.89%	53.89%	53.89%	53.89%	53.89%	53.89%
<b>U.S. GAAP:</b>						

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Total revenues	\$ 6,756	Ps. 72,959	Ps. 60,749	Ps. 53,544	Ps. 47,973	Ps. 43,298
Income from operations	698	7,536	6,662	5,793	5,184	5,339



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	Selected Consolidated Financial Information					
	2006 <sup>(1)</sup>	2006	2005	2004	2003 <sup>(2)</sup>	2002
	(In millions of U.S. dollars and millions of Mexican pesos at December 31, 2006, except for per share data, the weighted average number of shares outstanding and percentages)					
Participation in Coca-Cola FEMSA's earnings <sup>(5)</sup>	216	2,332	2,125	2,830	1,217	1,514
Minority interest	(15)	(163)		505	413	668
Net income	622	6,720	5,840	7,086	3,699	3,626
Net income: <sup>(6)</sup>						
Per Series B Share	0.03	0.34	0.30	0.40	0.21	0.20
Per Series D Share	0.04	0.42	0.38	0.50	0.26	0.25
Weighted average number of shares outstanding (in millions):						
Series B Shares	9,246.4	9,246.4	8,834.8	8,217.5	8,217.5	8,217.5
Series D Shares	8,644.7	8,644.7	8,260.1	7,683.0	7,683.0	7,683.0
<b>Balance Sheet Data:</b>						
<b>Mexican FRS:</b>						
Total assets	\$ 13,463	\$ 145,390	\$ 132,312	\$ 131,173	\$ 121,687	\$ 70,970
Current liabilities	2,346	25,337	20,960	25,630	19,717	13,946
Long-term debt <sup>(7)</sup>	3,172	34,251	30,942	39,038	37,898	11,527
Other long-term liabilities	1,071	11,574	9,921	9,862	10,948	6,637
Capital stock	477	5,154	5,154	4,799	4,799	4,799
Total stockholders' equity	6,874	74,228	70,489	56,643	53,124	38,860
Majority interest	5,021	54,220	50,027	38,322	32,925	27,208
Minority interest	1,853	20,008	20,462	18,321	20,199	11,652

**Table of Contents****Selected Consolidated Financial Information**

	Year Ended December 31,					
	2006 <sup>(1)</sup>	2006	2005	2004	2003 <sup>(2)</sup>	2002
(in millions of U.S. dollars and millions of Mexican pesos at December 31, 2006, except for						
per share data, the weighted average number of shares outstanding and percentages)						
<b>U.S. GAAP:</b>						
Total assets	\$ 10,235	Ps.110,538	Ps.95,286	Ps.89,257	Ps.77,898	Ps.75,274
Current liabilities	1,322	14,278	9,724	16,381	11,230	13,140
Long-term debt <sup>(7)</sup>	1,673	18,070	14,627	15,665	8,041	7,799
Other long-term liabilities	628	6,784	4,815	3,344	5,329	4,952
Minority interest	15	160	50	54	5,752	6,144
Capital stock	477	5,154	5,154	4,799	4,799	4,799
Stockholders equity	6,597	71,246	66,070	53,813	47,546	43,239
<b>Other information:</b>						
<b>Mexican FRS:</b>						
Depreciation <sup>(8)</sup>	\$ 426	Ps. 4,599	Ps. 4,382	Ps. 4,125	Ps. 3,614	Ps. 2,729
Capital expenditures <sup>(9)</sup>	823	8,888	7,034	7,508	7,722	6,542
Operating margin <sup>(10)</sup>	13.8%	13.8%	14.7%	14.6%	15.8%	17.5%
<b>U.S. GAAP:</b>						
Depreciation	\$ 193	Ps. 2,080	Ps. 2,038	Ps. 1,958	Ps. 2,262	Ps. 1,899
Operating margin <sup>(10)</sup>	10.3%	10.3%	11.0%	10.8%	10.8%	12.3%

- (1) Translation to U.S. dollar amounts at an exchange rate of Ps. 10.7995 to US\$ 1.00 solely for the convenience of the reader.
- (2) Our 2003 financial information is not comparable to prior and subsequent periods due to the acquisition of Panamco in May 2003 by our subsidiary Coca-Cola FEMSA. See Item 5 Operating and Financial Review and Prospectus Comparability of Information Presented-Panamco Acquisition.
- (3) Includes income tax, tax on assets and employee profit sharing.
- (4) The net income per Series B Share and per Series D Share was calculated in accordance with Bulletin B-14 *Utilidad por Acci3n* (Earnings per Share) of Mexican Financial Reporting Standards.
- (5) Coca-Cola FEMSA is included under the equity method for U.S. GAAP, as discussed in note 27 (a) to our audited consolidated financial statements.
- (6) Reflects 3-for-1 stock split effective May 28, 2007 in respect of our BD Units and May 30, 2007 in respect of our ADS, which is after the date of the latest reported balance sheet, but before the issuance of the consolidated financial statements included in this annual report as established by EITF D-86 ( Issuance of Financial Statements ). For US GAAP purposes, FASB No. 128 Earnings per Share establishes that the earnings-per-share computation as of December 31, 2006 and previous year computations should be based on the new number of shares following the stock split. See Item 5 Operating and Financial Review and Prospectus Recent Developments.
- (7) Includes long-term debt minus the current portion of long-term debt.
- (8) Includes bottle breakage for Coca-Cola FEMSA.

(9) Includes investments in property, plant and equipment, intangible and other assets.

(10) Operating margin is calculated by dividing income from operations by total revenues.

**Dividends**

We have historically paid dividends per BD Unit (including in the form of ADSs) approximately equal to or greater than 1% of the market price on the date of declaration, subject to changes in our results of operations and financial position, including due to extraordinary economic events and to the factors described in Risk Factors that affect our financial condition and liquidity. These factors may affect whether or not dividends are declared and the amount of such dividends. We do not expect to be subject to any contractual restrictions on our ability to pay dividends, although our subsidiaries may be subject to such restrictions. Because we are a holding company with no significant operations of our own, we will have distributable profits and cash to pay dividends only to the

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extent that we receive dividends from our subsidiaries. Accordingly, we cannot assure you that we will pay dividends or as to the amount of any dividends.

The following table sets forth for each year the nominal amount of dividends per share that we declared in Mexican pesos and the U.S. dollar amounts that were actually paid on each of the respective payment dates for the 2002 to 2006 fiscal years:

Date Dividend Paid	Fiscal Year with Respect to which	Dividend was Declared	Aggregate Amount of Dividend Declared <sup>(1)</sup>	Per Series B Share Dividend	Per Series B Share Dividend	Per Series D Share Dividend	Per Series D Share Dividend
May 30, 2003	2002	Ps.	397,792,604	Ps.0.0670	\$ 0.0065	Ps. 0.0838	\$ 0.0081
May 31, 2004	2003	Ps.	531,379,672	Ps.0.0895	\$ 0.0078	Ps. 0.1119	\$ 0.0098
May 31, 2005	2004	Ps.	659,997,941	Ps.0.1112	\$ 0.0102	Ps. 0.1389	\$ 0.0127
June 15, 2006	2005	Ps.	986,000,000	Ps.0.1475	\$ 0.0129	Ps. 0.1844	\$ 0.0161
May 15, 2007	2006	Ps.	1,485,000,000	Ps.0.2222	\$ 0.0206	Ps. 0.2777	\$ 0.0257

<sup>(1)</sup> The aggregate amount of dividend declared is determined by the per series dividend amount multiplied by (a), for 2002 through 2004, 2,737,740,090 Series B Shares and 2,559,570,360 Series D Shares, and (b), for 2005 and 2006, 3,082,140,090 Series B Shares and 2,881,570,360 Series D Shares, which is in each case the number of shares outstanding at the date each dividend is declared.

At the annual ordinary general shareholders meeting, the board of directors submits the financial statements of our company for the previous fiscal year, together with a report thereon by the board of directors. Once the holders of Series B Shares have approved the financial statements, they determine the allocation of our net profits for the preceding year. Mexican law requires the allocation of at least 5% of net profits to a legal reserve, which is not subsequently available for distribution, until the amount of the legal reserve equals 20% of our paid in capital stock. Thereafter, the holders of Series B Shares may determine and allocate a certain percentage of net profits to any general or special reserve, including a reserve for open-market purchases of our shares. The remainder of net profits is available for distribution in the form of dividends to our shareholders. Dividends may only be paid if net profits are sufficient to offset losses from prior fiscal years.

Our bylaws provide that, before May 11, 2008, dividends will be allocated among the shares outstanding and fully paid at the time a dividend is declared in such manner that each Series D-B Share and Series D-L Share receives 125% of the dividend distributed in respect of each Series B Share. Holders of Series D-B Shares and Series D-L Shares are entitled to this dividend premium in connection with all dividends paid by us other than payments in connection with the liquidation of our company. On May 11, 2008, the Series D-B Shares will automatically convert into Series B Shares and the Series D-L Shares will automatically convert into Series L Shares, which will not be entitled to a dividend premium. From and after May 11, 2008, the Series L Shares and Series B Shares that are outstanding and fully paid at the time a dividend is declared will be entitled to share equally in the dividend.

Subject to certain exceptions contained in the deposit agreement dated May 11, 2007, among FEMSA, The Bank of New York, as ADS depository, and holders and beneficial owners from time to time of our American Depositary Shares, or ADSs, evidenced by American Depositary Receipts, any dividends distributed to holders of our ADSs will be paid to the ADS depository in Mexican pesos and will be converted by the ADS depository into U.S. dollars. As a result, restrictions on conversion of Mexican pesos into foreign currencies and exchange rate fluctuations may affect the ability of holders of our ADSs to receive U.S. dollars and the U.S. dollar amount actually received by holders of our ADSs. Although the Mexican government does not currently restrict the ability of Mexican and foreign persons or entities to convert Mexican pesos to U.S. dollars or other currencies or to transfer other currencies out of Mexico, we cannot give any assurance that the Mexican government will not institute a restrictive exchange control policy in the future.

**Table of Contents****Exchange Rate Information**

The following tables set forth, for the periods indicated, the high, low, average and period end noon buying rates of the Federal Reserve Bank of New York, expressed in Mexican pesos per one U.S. dollar. The rates have not been restated in constant currency units and therefore represent nominal historical figures.

Period	Exchange Rate			Period End
	High	Low	Average <sup>(1)</sup>	
2002	10.43	9.00	9.66	10.43
2003	11.41	10.11	10.80	11.24
2004	11.64	10.81	11.29	11.15
2005	11.41	10.41	10.89	10.63
2006	11.46	10.43	10.91	10.80

(1) Average month-end rates.

Period	Exchange Rate		
	High	Low	Period End
2005:			
First Quarter	Ps. 11.41	Ps. 10.98	Ps. 11.18
Second Quarter	11.23	10.76	10.77
Third Quarter	10.90	10.58	10.79
Fourth Quarter	10.94	10.41	10.63
2006:			
First Quarter	Ps. 10.95	Ps. 10.46	Ps. 10.90
Second Quarter	11.46	10.84	11.29
Third Quarter	11.18	10.74	10.98
Fourth Quarter	11.06	10.71	10.80
December	10.99	10.77	10.80
2007:			
January	Ps. 11.09	Ps. 10.77	Ps. 11.04
February	11.16	10.92	11.16
March	11.18	11.01	11.04
April	11.03	10.92	10.93
May	10.93	10.74	10.74
June <sup>(1)</sup>	10.98	10.71	10.81

(1) From the period beginning June 1 until June 15, 2007.

Mexico has a free foreign exchange market and, since December 1994, the Mexican government has not intervened to maintain the value of the Mexican peso against the U.S. dollar. The Mexican peso declined in 1998 as the foreign exchange markets experienced volatility as a result of the financial crises in Asia and Russia and the financial turmoil in countries such as Brazil and Venezuela. The Mexican peso remained relatively stable from 1999 until the fall of 2001. In late 2001 and early 2002, the Mexican peso appreciated considerably against the U.S. dollar and, more strongly, against other foreign currencies. From the second quarter of 2002 and until the end of 2003, the Mexican peso depreciated in value. The Mexican peso has remained relatively stable since 2004. The Mexican government may not maintain its current policies with regard to the Mexican peso and, accordingly, the Mexican peso may depreciate significantly in the future.

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**RISK FACTORS**

**Risks Related to Our Company**

**Coca-Cola FEMSA**

*Coca-Cola FEMSA's business depends on its relationship with The Coca-Cola Company, and changes in this relationship may adversely affect its results of operations and financial position.*

Approximately 95% of Coca-Cola FEMSA's sales volume in 2006 was derived from sales of Coca-Cola trademark beverages. In each of its territories, Coca-Cola FEMSA produces, markets and distributes Coca-Cola trademark beverages through standard bottler agreements. Through its rights under the bottler agreements and as a large shareholder, The Coca-Cola Company has the ability to exercise substantial influence over the conduct of Coca-Cola FEMSA's business.

Under Coca-Cola FEMSA's bottler agreements, The Coca-Cola Company may unilaterally set the price for its concentrate. In 2005, The Coca-Cola Company decided to gradually increase concentrate prices for carbonated soft drinks over a three year period in Mexico beginning in 2007 and in Brazil in 2006. Coca-Cola FEMSA prepares a three-year general business plan that is submitted to its board of directors for approval. The Coca-Cola Company may require that Coca-Cola FEMSA demonstrate its financial ability to meet its plans and may terminate Coca-Cola FEMSA's rights to produce, market and distribute soft drinks in territories with respect to which such approval is withheld. The Coca-Cola Company also makes significant contributions to Coca-Cola FEMSA's marketing expenses although it is not required to contribute a particular amount. In addition, Coca-Cola FEMSA is prohibited from bottling any soft drink product or distributing other beverages without The Coca-Cola Company's authorization or consent. Coca-Cola FEMSA may not transfer control of the bottler rights of any of its territories without the consent of The Coca-Cola Company.

Coca-Cola FEMSA depends on The Coca-Cola Company to renew its bottler agreements. Coca-Cola FEMSA's bottler agreements for Mexico expire in 2013 and 2015 and are renewable in each case for ten-year terms. Coca-Cola FEMSA's bottler agreements for Brazil expired in December 2004 and for Venezuela in August 2006. Coca-Cola FEMSA and its bottler agreements for Guatemala, Nicaragua, Panama (other beverages) and Colombia expire in June 2007. Coca-Cola FEMSA's bottler agreement for *Coca-Cola* trademark beverages for Panama has an indefinite term but may be terminated with six months prior written notice by either party. Coca-Cola FEMSA is currently in the process of negotiating renewals of these agreements on similar terms and conditions as in other countries. Coca-Cola FEMSA's remaining territories are governed by bottler agreements that expire after June 2007. There can be no assurances that The Coca-Cola Company will decide to renew any of these agreements. In addition, in the event a material breach of these agreements occurs, the agreements may be terminated. Termination would prevent Coca-Cola FEMSA from selling Coca-Cola trademark beverages in the affected territory and would have an adverse effect on Coca-Cola FEMSA's business, financial condition, prospects and results of operations

*The Coca-Cola Company has substantial influence on the conduct of Coca-Cola FEMSA's business, which may result in Coca-Cola FEMSA taking actions contrary to the interest of its remaining shareholders.*

The Coca-Cola Company has significant influence on the conduct of Coca-Cola FEMSA's business. The Coca-Cola Company indirectly owns 31.6% of Coca-Cola FEMSA's outstanding capital stock, representing 37.0% of its capital stock with full voting rights. The Coca-Cola Company is entitled to appoint four of Coca-Cola FEMSA's 18 directors and certain of its executive officers and, except under limited circumstances, has the power to veto all actions requiring approval by Coca-Cola FEMSA's board of directors. We indirectly own 53.7% of Coca-Cola FEMSA's outstanding capital stock, representing 63.0% of Coca-Cola FEMSA's capital stock with full voting rights. We are entitled to appoint 11 of Coca-Cola FEMSA's 18 directors and certain of its

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executive officers. The Coca-Cola Company, thus may have the power to determine the outcome of actions requiring approval by its board of directors and may have the power to determine the outcome of actions requiring approval of Coca-Cola FEMSA's shareholders. See Item 10. Additional Information Material Contracts Coca-Cola FEMSA. The interests of The Coca-Cola Company may be different from the interests of Coca-Cola FEMSA's remaining shareholders, which may result in Coca-Cola FEMSA taking actions contrary to the interest of its remaining shareholders.

***Coca-Cola FEMSA has significant transactions with affiliates, particularly The Coca-Cola Company, which may create potential conflicts of interest and could result in less favorable terms to Coca-Cola FEMSA.***

Coca-Cola FEMSA engages in transactions with subsidiaries of The Coca-Cola Company, including cooperative marketing arrangements and a number of bottler agreements. Coca-Cola FEMSA agreed jointly with The Coca-Cola Company to purchase 100% of the outstanding shares of Jugos del Valle, S.A.B de C.V., which we refer to as Jugos del Valle, a Mexican juice and beverage producer. See Item 5. Operating and Financial Review and Prospectus Recent Developments. In addition, Coca-Cola FEMSA has entered into cooperative marketing arrangements with The Coca-Cola Company. The transactions may create potential conflicts of interest, which could result in terms less favorable to Coca-Cola FEMSA than could be obtained from an unaffiliated third party.

***Competition could adversely affect Coca-Cola FEMSA's financial performance.***

The beverage industry throughout Latin America is highly competitive. Coca-Cola FEMSA faces competition from other bottlers of carbonated soft drinks such as Pepsi products, and from producers of low cost beverages, or B brands. Coca-Cola FEMSA also competes against beverages other than soft drinks such as water, fruit juice and sport drinks. In Mexico, Coca-Cola FEMSA faces competition from water beverage companies such as Danone, with its local brand Aguas Santa María, from Pepsico in the sport drink market, with its Gatorade brand, and from a diverse array of local fruit juice beverage companies. Although competitive conditions are different in each of Coca-Cola FEMSA's territories, Coca-Cola FEMSA competes principally in terms of price, packaging, consumer sale promotions, customer service and non-price retail incentives. There can be no assurances that Coca-Cola FEMSA will be able to avoid lower pricing as a result of competitive pressure. Lower pricing, changes made in response to competition and changes in consumer preferences may have an adverse effect on Coca-Cola FEMSA's financial performance.

Coca-Cola FEMSA's principal competitor in Mexico is The Pepsi Bottling Group, or PBG. PBG is the largest bottler of Pepsi products worldwide and competes with Coca-Cola trademark beverages. Coca-Cola FEMSA has also experienced stronger competition in Mexico from lower priced soft drinks in larger, multiple serving packaging. In Argentina and Brazil, Coca-Cola FEMSA competes with Companhia de Bebidas das Américas, commonly referred to as AmBev, the largest brewer in Latin America and a subsidiary of InBev S.A., which sells Pepsi products, in addition to a portfolio that includes local brands with flavors such as guaraná and proprietary beers. In each of its territories, Coca-Cola FEMSA competes with Pepsi bottlers and with various other bottlers and distributors of nationally and regionally advertised soft drinks.

***A water shortage or a failure to maintain existing concessions could adversely affect Coca-Cola FEMSA's business.***

Water is an essential component of soft drinks. Coca-Cola FEMSA obtains water from various sources in its territories, including springs, wells, rivers and municipal water companies. In Mexico, Coca-Cola FEMSA purchases water from municipal water companies and pumps water from its own wells pursuant to concessions granted by the Mexican government. Coca-Cola FEMSA obtains the vast majority of the water used in its soft

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drink production in Mexico pursuant to these concessions, which the Mexican government granted based on studies of the existing and projected groundwater supply. Coca-Cola FEMSA's existing water concessions in Mexico may be terminated by governmental authorities under certain circumstances and their renewal depends on receiving necessary authorizations from municipal and/or federal water authorities. See Item 4 Information on the Company Regulatory Matters Water Supply Law. In Coca-Cola FEMSA's other territories, its existing water supply may not be sufficient to meet its future production needs and the available water supply may be adversely affected by shortages or changes in governmental regulations.

Coca-Cola FEMSA cannot assure you that water will be available in sufficient quantities to meet its future production needs or will prove sufficient to meet its water supply needs.

***Increases in the prices of raw materials would increase Coca-Cola FEMSA's cost of sales and may adversely affect its results of operations.***

Coca-Cola FEMSA's most significant raw materials are concentrate, which it acquires from companies designated by The Coca-Cola Company, packaging materials and sweeteners. Prices for concentrate are determined by The Coca-Cola Company pursuant to Coca-Cola FEMSA's bottler agreements as a percentage of the weighted average retail price in local currency, net of applicable taxes. In 2005, The Coca-Cola Company decided to gradually increase concentrate prices for carbonated soft drinks over a three-year period in Mexico which began in 2007 and in Brazil in 2006. The prices for Coca-Cola FEMSA's remaining raw materials are driven by market prices and local availability as well as the imposition of import duties and import restrictions and fluctuations in exchange rates. Coca-Cola FEMSA is also required to meet all of its supply needs from suppliers approved by The Coca-Cola Company, which may limit the number of suppliers available to it. Coca-Cola FEMSA's sales prices are denominated in the local currency in which it operates, while the prices of certain materials used in the bottling of its products, mainly resin and ingots to make plastic bottles, finished plastic bottles and aluminum cans, are paid in or determined with reference to the U.S. dollar, and therefore may increase if the U.S. dollar appreciates against the currency of any country in which Coca-Cola FEMSA operates, particularly against the Mexican peso. See Item 4 Information on the Company Coca-Cola FEMSA Raw Materials.

Coca-Cola FEMSA's most significant packaging raw material costs arise from the purchase of resin and plastic ingots to make plastic bottles and from the purchase of finished plastic bottles, the prices of which are tied to crude oil prices and global resin supply. In Mexico, the U.S. dollar prices that Coca-Cola FEMSA paid for resin remained relatively flat in 2006. Sugar prices in all of the countries in which Coca-Cola FEMSA operates other than Brazil are subject to local regulations and other barriers to market entry that cause it to pay in excess of international market prices for sugar. Coca-Cola FEMSA expects sugar prices to decrease in 2007 in all of the countries in which it operates other than Mexico and Venezuela. In Venezuela, Coca-Cola FEMSA has experienced sugar shortages that have adversely affected its operations. These shortages were due to insufficient domestic production to meet demand and current restrictions on sugar imports.

Coca-Cola FEMSA cannot assure you that its raw material prices will not further increase in the future. Increases in the prices of raw materials would increase Coca-Cola FEMSA's cost of sales and adversely affect its results of operations.

***Taxes on soft drinks could adversely affect Coca-Cola FEMSA's business.***

Coca-Cola FEMSA's products are subject to excise and value-added taxes in many of the countries in which it operates. The imposition of new taxes or increases in taxes on its products may have a material adverse effect on Coca-Cola FEMSA's business, financial condition, prospects and results of operations. In 2003, Mexico implemented a 20% excise tax on carbonated soft drinks produced with non-sugar sweetener. This tax was eliminated beginning in 2007. Certain countries in Central America, Argentina and Brazil impose taxes on



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carbonated soft drinks. See Item 4 Information on the Company Coca-Cola FEMSA Taxation of Soft Drinks. We cannot assure you that any governmental authority in any country where Coca-Cola FEMSA operates will not impose or increase taxes on its products in the future.

### ***Regulatory developments may adversely affect Coca-Cola FEMSA's business.***

Coca-Cola FEMSA is subject to regulation in each of the territories in which it operates. The principal areas in which Coca-Cola FEMSA is subject to regulation are environment, labor, taxation, health and antitrust. The adoption of new laws or regulations in the countries in which Coca-Cola FEMSA operates may increase its operating costs or impose restrictions on its operations which, in turn, may adversely affect its financial condition, business and results of operations. In particular, environmental standards are becoming more stringent in several of the countries in which Coca-Cola FEMSA operates, and Coca-Cola FEMSA is in the process of complying with these new standards. Further changes in current regulations may result in an increase in compliance costs, which may have an adverse effect on Coca-Cola FEMSA's future results of operations or financial condition.

Voluntary price restraints or statutory price controls have been imposed historically in several of the countries in which Coca-Cola FEMSA operates. The imposition of these restrictions in the future may have an adverse effect on Coca-Cola FEMSA's results of operations and financial position. Although Mexican bottlers have been free to set prices for carbonated soft drinks without governmental intervention since January 1996, such prices had been subject to statutory price controls and to voluntary price restraints, which effectively limited Coca-Cola FEMSA's ability to increase prices in the Mexican market without governmental consent. We cannot assure that governmental authorities in any country where Coca-Cola FEMSA operates will not impose statutory price controls or voluntary price restraints in the future.

Coca-Cola FEMSA's operations have from time to time been subject to investigations and proceedings by antitrust authorities and litigation relating to alleged anticompetitive practices. We cannot assure you that these investigations and proceedings will not have an adverse effect on Coca-Cola FEMSA's results of operations or financial condition.

## **FEMSA Cerveza**

### ***Unfavorable economic conditions in Mexico, Brazil or the United States may adversely affect FEMSA Cerveza's business.***

Demand for the products of FEMSA Cerveza may be affected by economic conditions in Mexico, Brazil or the United States. In particular, demand in northern Mexico, where there are a large number of border towns, may be disproportionately affected by the performance of the United States' economy. In addition, FEMSA Cerveza's exports to the United States may be affected by reduced demand from the United States or from a reduction in prices by its competitors. Any depreciation of the Mexican peso may negatively affect its results of operations because a significant portion of its costs and expenses are denominated in, or determined by reference to, the U.S. dollar.

### ***Uncertainty in commodity prices of raw materials used by FEMSA Cerveza may result in increased costs and adversely affect its results of operations.***

FEMSA Cerveza purchases a number of commodities for the production of its products (principally aluminum, barley, malt and hops) from Mexican producers and in the international market. The prices of such commodities can fluctuate and are determined by global supply and demand and other factors, including changes in exchange rates, over which FEMSA Cerveza has no control. Market prices for aluminum increased by approximately 35% in 2006. Because aluminum prices are denominated in U.S. dollars, an appreciation of the U.S. dollar against the Mexican peso would increase the cost to FEMSA Cerveza as a percentage of net sales, as

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its sales are generally in Mexican pesos. There can be no assurance that FEMSA Cerveza will be able to recover increases in the cost of raw materials. See Item 4. Information on the Company FEMSA Cerveza Raw Materials. An increase in raw materials costs would adversely affect its results of operations.

### ***FEMSA Cerveza's sales in the United States depend on distribution arrangements with Heineken USA.***

Heineken USA Inc., or Heineken USA, is the exclusive importer, marketer and distributor of FEMSA Cerveza's beer brands in the United States under a three-year agreement that expires on December 31, 2007. In addition, in April 2007 FEMSA Cerveza and Heineken USA entered into a new ten-year agreement pursuant to which Heineken USA will continue to be the exclusive importer, marketer and distributor of FEMSA Cerveza's beer brands in the United States. Accordingly, FEMSA Cerveza's exports to the United States depend to a significant extent on Heineken USA's performance under these agreements. See Item 5. Operating and Financial Review and Prospectus Recent Developments. We cannot assure that Heineken USA will be able to maintain or increase sales of FEMSA Cerveza's beer brands in the United States, nor that when the new agreement expires in December of 2017, FEMSA Cerveza will be able to renew the agreement or enter into a substitute arrangement on comparable terms.

### ***FEMSA Cerveza's sales in the Mexican market depend on its ability to compete with Grupo Modelo.***

FEMSA Cerveza faces competition in the Mexican beer market from Grupo Modelo, S.A. de C.V., or Grupo Modelo. FEMSA Cerveza's ability to compete successfully in the Mexican beer market will have a significant impact on its Mexican sales. See Item 4. Information on the Company FEMSA Cerveza The Mexican Beer Market.

### ***FEMSA Cerveza's sales in the Brazilian market depend on its ability to compete with local brewers.***

FEMSA Cerveza faces competition in the Brazilian beer market from Companhia de Bebidas das Americas, or AmBev, Grupo Schincariol and Cervejarias Petropolis. FEMSA Cerveza's ability to compete successfully in the Brazilian beer market will have a significant impact on its Brazilian sales. See Item 4. Information on the Company FEMSA Cerveza The Brazilian Beer Market.

### ***Competition from imports in the Mexican beer market is increasing and may adversely affect FEMSA Cerveza's business.***

Imports represented 2.1% of the Mexican beer market in terms of sales volume in 2006. Under the North American Free Trade Agreement, or NAFTA, the tariffs applicable to beers imported from the United States and Canada were eliminated in January 2001. Increased import competition, however, could result from potential new entrants to the Mexican beer market or from a change in consumer preferences in Mexico and could lead to greater competition in general, which may adversely affect FEMSA Cerveza's business, financial position and results of operations. See Item 4. Information on the Company FEMSA Cerveza The Mexican Beer Market.

### ***Regulatory developments in our main markets could adversely affect FEMSA Cerveza's business.***

FEMSA Cerveza's business is subject to a variety of different government regulations in our key markets of Mexico, Brazil and the United States, and thus may be affected by changes in law, regulation or regulatory policy. Particularly in Mexico, actions of federal and local authorities, specifically changes in governmental policy with respect to excise and value-added tax laws or cold beer regulation and governmental actions relating to the beer industry practice of tied-customer arrangements, which are agreements with retailers to sell and promote a beer producer's products, may have a material adverse effect on FEMSA Cerveza's business, financial position and results of operations.

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Federal regulation of beer consumption in Mexico is primarily effected through a 25% excise tax, which starting January 2006 includes an alternative minimum Mexican peso amount of Ps. 3.00 per liter for non-returnable presentations and Ps. 1.74 per liter for returnable presentations, and a 15% value-added tax. Currently, we do not anticipate an increase in these taxes, but federal regulation relating to excise taxes may change in the future, resulting in an increase or decrease in the tax. Local regulations are primarily effected through the issuance of licenses authorizing retailers to sell alcoholic beverages. Other regulations affecting beer consumption in Mexico vary according to local jurisdictions and include limitations on the hours during which restaurants, bars and other retail outlets are allowed to sell beer. See Item 4. Information on the Company FEMSA Cerveza The Mexican Beer Market.

### ***FEMSA Cerveza may not be able to improve performance in its newly acquired Brazilian operations.***

In 2006, FEMSA Cerveza acquired through a series of transactions 99.83% of Brazilian brewer Cervejarias Kaiser Brasil S.A., or Kaiser. Prior to the acquisition, Kaiser's profitability and market position had declined as a result of operational changes by the prior owner and increased competition in the Brazilian beer market. Kaiser's operating margins are therefore lower than those of FEMSA Cerveza's Mexican operations. FEMSA Cerveza is currently in the process of implementing a number of initiatives to seek to improve Kaiser's performance, although FEMSA Cerveza has not previously conducted operations in the Brazilian beer market, where market conditions differ significantly from Mexico. FEMSA Cerveza's initiatives may not be successful in improving Kaiser's performance, which would adversely affect FEMSA Cerveza's sales growth and operating margins.

### ***A water supply shortage could adversely affect FEMSA Cerveza's business.***

FEMSA Cerveza purchases water from Mexican government entities and obtains pump water from its own wells pursuant to concessions granted by the Mexican government.

FEMSA Cerveza believes that its water concessions will satisfy its current and future water requirements. We cannot assure, however, that isolated periods of adverse weather will not affect FEMSA Cerveza's supply of water to meet its future production needs in any given period, or that its concessions will not be terminated or will be renewed by the Mexican government. Any of these events or actions may adversely affect FEMSA Cerveza's business, financial position and results of operations.

## **FEMSA Comercio**

### ***Competition from other retailers in Mexico could adversely affect FEMSA Comercio's business.***

The Mexican retail sector is highly competitive. FEMSA participates in the retail sector primarily through FEMSA Comercio. FEMSA Comercio's Oxxo convenience stores face competition on a regional basis from 7-Eleven, Super Extra, Super City, AM/PM and Circle K stores, among others. In particular, the Super Extra chain is owned and managed by Grupo Modelo, our main competitor in the Mexican beer market, and since 2003 Super Extra has aggressively expanded the number of its stores. Oxxo convenience stores also face competition from numerous small chains of retailers across Mexico. In the future, Oxxo stores may face additional competition from other retailers that do not currently participate in the convenience store sector or from new market entrants. Increased competition may limit the number of new locations available to FEMSA Comercio and require FEMSA Comercio to modify its product offering or pricing. In addition, consumers may prefer alternative products or store formats offered by competitors. As a result, FEMSA Comercio's results of operations and financial position may be adversely affected by competition in the future.

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### ***Sales of Oxxo convenience stores may be adversely affected by changes in economic conditions in Mexico.***

Convenience stores often sell certain products at a premium. The convenience store market is thus highly sensitive to economic conditions, since an economic slowdown is often accompanied by a decline in consumer purchasing power, which in turn results in a decline in the overall consumption of FEMSA Comercio's main product categories. During periods of economic slowdown, Oxxo stores may experience a decline in traffic per store and purchases per customer, and this may result in a decline in FEMSA Comercio's results of operations.

### ***FEMSA Comercio may not be able to maintain its historic growth rate.***

FEMSA Comercio increased the number of Oxxo stores at an average annual rate of 21.6% from 2002 to 2006. The growth in the number of Oxxo stores has driven growth in total revenue and operating income at FEMSA Comercio over the same period. As the overall number of stores increases, percentage growth in the number of Oxxo stores is likely to decrease. In addition, as convenience store penetration in Mexico grows, the number of viable new store locations may decrease, and new store locations may be less favorable in terms of same store sales, average ticket and store traffic. As a result, FEMSA Comercio's future results of operations and financial condition may not be consistent with prior periods and may be characterized by lower growth rates in terms of total revenue and operating income.

### **Risks Related to Our Principal Shareholders and Capital Structure**

#### ***A majority of our voting shares are held by a voting trust, which effectively controls the management of our company, and whose interests may differ from those of other shareholders.***

As of May 31, 2007, a voting trust, the participants of which are members of five families, owned 38.64% of our capital stock and 74.78% of our capital stock with full voting rights, consisting of the Series B Shares. Consequently, the voting trust has the power to elect a majority of the members of our board of directors and to play a significant or controlling role in the outcome of substantially all matters to be decided by our board of directors or our shareholders. The interests of the voting trust may differ from those of our other shareholders. See Item 7. Major Shareholders and Related Party Transactions and Item 10. Additional Information Bylaws Voting Rights and Certain Minority Rights.

#### ***Holders of Series D-B and D-L Shares have limited voting rights.***

Holders of Series D-B and D-L Shares have limited voting rights and are only entitled to vote on specific matters, such as changes in the form of our corporate organization (other than a change from a *sociedad anónima bursátil de capital variable* to a *sociedad anónima bursátil*, and vice versa), dissolutions, liquidations a merger with a company with a distinct corporate purpose, cancellation of the registration of the Series D-B and D-L Shares and any other matters that expressly require approval from such holders under the new Mexican Securities Market Law, which we refer to as the Mexican Securities Law. As a result of these limited voting rights, Series D-B and D-L these holders will not be able to influence our business or operations. See Item 7. Major Shareholders and Related Party Transactions Major Shareholders and Item 10. Additional Information Bylaws Voting Rights and Certain Minority Rights.

#### ***Holders of ADSs may not be able to vote at our shareholder meetings.***

Our shares are traded on the New York Stock Exchange in the form of ADSs. We cannot assure that holders of our shares in the form of ADSs will receive notice of shareholders' meetings from our ADS depository in sufficient time to enable such holders to return voting instructions to the ADS depository in a timely manner. In the event that instructions are not received with respect to any shares underlying ADSs, the ADS depository will, subject to certain limitations, grant a proxy to a person designated by us in respect of these shares. In the event

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that this proxy is not granted, the ADS depository will vote these shares in the same manner as the majority of the shares of each class for which voting instructions are received.

***Holders of BD Units in the United States and holders of ADSs may not be able to participate in any future preemptive rights offering and as a result may be subject to dilution of their equity interests.***

Under applicable Mexican law, if we issue new shares for cash as a part of a capital increase, other than in connection with a public offering of newly issued shares or treasury stock (which are exempted under the Mexican Securities Law), we are generally required to grant our shareholders the right to purchase a sufficient number of shares to maintain their existing ownership percentage. Rights to purchase shares in these circumstances are known as preemptive rights. We may not legally allow holders of our shares or ADSs who are located in the United States to exercise any preemptive rights in any future capital increases unless (1) we file a registration statement with the SEC with respect to that future issuance of shares or (2) the offering qualifies for an exemption from the registration requirements of the U.S. Securities Act of 1933. At the time of any future capital increase, we will evaluate the costs and potential liabilities associated with filing a registration statement with the SEC, as well as the benefits of preemptive rights to holders of our shares in the form of ADSs in the United States and any other factors that we consider important in determining whether to file a registration statement.

We may decide not to file a registration statement with the SEC to allow holders of our shares or ADSs who are located in the United States to participate in a preemptive rights offering. In addition, under current Mexican law, the sale by the ADS depository of preemptive rights and the distribution of the proceeds from such sales to the holders of our shares in the form of ADSs is not possible. As a result, the equity interest of holders of our shares in the form of ADSs would be diluted proportionately. See Item 10. Additional Information Preemptive Rights.

***The protections afforded to minority shareholders in Mexico are different from those afforded to minority shareholders in the United States.***

Under Mexican law, the protections afforded to minority shareholders are different from, and may be less than, those afforded to minority shareholders in the United States. Mexican laws do not provide a remedy to shareholders relating to violations of fiduciary duties, there is no procedure for class actions as such actions are conducted in the United States and there are different procedural requirements for bringing shareholder lawsuits against directors for the benefit of companies. Therefore, it may be more difficult for minority shareholders to enforce their rights against us, our directors or our controlling shareholders than it would be for minority shareholders of a United States company.

***Investors may experience difficulties in enforcing civil liabilities against us or our directors, officers and controlling persons.***

FEMSA is organized under the laws of Mexico, and most of our directors, officers and controlling persons reside outside the United States. In addition, all or a substantial portion of our assets and their respective assets are located outside the United States. As a result, it may be difficult for investors to effect service of process within the United States on such persons or to enforce judgments against them, including any action based on civil liabilities under the U.S. federal securities laws. There is doubt as to the enforceability against such persons in Mexico, whether in original actions or in actions to enforce judgments of U.S. courts, of liabilities based solely on the U.S. federal securities laws.

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### ***Developments in other countries may adversely affect the market for our securities.***

The market value of securities of Mexican companies are, to varying degrees, influenced by economic and securities market conditions in other emerging market countries. Although economic conditions are different in each country, investors' reaction to developments in one country can have effects on the securities of issuers in other countries, including Mexico. We cannot assure you that events elsewhere, especially in emerging markets, will not adversely affect the market value of our securities.

### ***The failure or inability of our subsidiaries to pay dividends or other distributions to us may adversely affect us and our ability to pay dividends to holders of ADSs.***

FEMSA is a holding company. Accordingly, FEMSA's cash flows are principally derived from dividends, interest and other distributions made to FEMSA by its subsidiaries. Currently, FEMSA's subsidiaries do not have contractual obligations that require them to pay dividends to FEMSA. In addition, debt and other contractual obligations of our subsidiaries may in the future impose restrictions on our subsidiaries' ability to make dividend or other payments to FEMSA, which in turn may adversely affect FEMSA's ability to pay dividends to shareholders and meet its debt and other obligations.

### **Risks Related to Mexico and the Other Countries in Which We Operate**

#### ***Adverse economic conditions in Mexico may adversely affect our financial position and results of operations.***

We are a Mexican corporation, and our Mexican operations are our single most important geographic segment. For the year ended December 31, 2006, 78% of our consolidated total revenues were attributable to Mexico. In the past, Mexico has experienced both prolonged periods of weak economic conditions and deteriorations in economic conditions that have had a negative impact on our company. We cannot assume that such conditions will not return or that such conditions will not have a material adverse effect on our results of operations and financial position.

Our business may be significantly affected by the general condition of the Mexican economy, or by the rate of inflation in Mexico, interest rates in Mexico and exchange rates for, or exchange controls affecting, the Mexican peso. Decreases in the growth rate of the Mexican economy, periods of negative growth and/or increases in inflation or interest rates may result in lower demand for our products, lower real pricing of our products or a shift to lower margin products. Because a large percentage of our costs and expenses are fixed, we may not be able to reduce costs and expenses upon the occurrence of any of these events, and our profit margins may suffer as a result. In addition, an increase in interest rates in Mexico would increase the cost to us of variable rate debt, which constituted 19.6% of our total debt as of December 31, 2006 (including the effect of interest rate swaps), and have an adverse effect on our financial position and results of operations.

#### ***Depreciation of the Mexican peso relative to the U.S. dollar could adversely affect our financial position and results of operations.***

A depreciation of the Mexican peso relative to the U.S. dollar would increase the cost to us of a portion of the raw materials we acquire, the price of which is paid in or determined with reference to U.S. dollars, and of our debt obligations denominated in U.S. dollars and thereby may negatively affect our financial position and results of operations. We generally do not hedge our exposure to the U.S. dollar with respect to the Mexican peso and other currencies. A severe devaluation or depreciation of the Mexican peso may also result in disruption of the international foreign exchange markets and may limit our ability to transfer or to convert Mexican pesos into U.S. dollars and other currencies for the purpose of making timely payments of interest and principal on our U.S.

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dollar-denominated debt or obligations in other currencies. While the Mexican government does not currently restrict, and since 1982 has not restricted, the right or ability of Mexican or foreign persons or entities to convert Mexican pesos into U.S. dollars or to transfer other currencies out of Mexico, the Mexican government could institute restrictive exchange rate policies in the future, as it has done in the past. Currency fluctuations may have an adverse effect on our financial position, results of operations and cash flows in future periods.

### ***Political events in Mexico could adversely affect our operations.***

Political events in Mexico may significantly affect our operations. In the Mexican federal elections held on July 2, 2000, Vicente Fox of the Partido Acción Nacional (the National Action Party) or PAN, won the presidency. Although his victory ended more than 70 years of presidential rule by the Partido Revolucionario Institucional (the Institutional Revolutionary Party) or PRI, neither the PRI nor the PAN succeeded in securing a majority in the Mexican congress. In elections in 2003 and 2004, the PAN lost additional seats in the Mexican congress and state governorships.

The July 2006 Mexican elections resulted in a change in administration, as presidential reelection is not permitted in Mexico. Felipe Calderón of the incumbent PAN party was elected President by a narrow margin, and the election results were challenged by the losing Partido de la Revolución Democrática (the Democratic Revolution Party) or PRD. The results were verified and ratified by all relevant formalities and President Calderón took office on December 1, 2006. The PAN controls a large percentage of the seats in both Federal legislative bodies, but requires building alliances with other parties to pass new laws and structural reforms. Potential legislative gridlock may adversely affect economic conditions in Mexico, and consequently, our results of operations.

### ***Developments in other Latin American countries in which we operate may adversely affect our business.***

In addition to conducting operations in Mexico, our subsidiary Coca-Cola FEMSA conducts operations in Guatemala, Nicaragua, Costa Rica, Panama, Colombia, Venezuela, Brazil and Argentina and, beginning in 2006, our subsidiary FEMSA Cerveza also conducts operations in Brazil. These countries expose us to different or greater country risk than Mexico. For some of these countries, results of operations in recent years have been adversely affected by deteriorating macroeconomic and political conditions. In Venezuela, significant economic, legal and political instability, including currency devaluation, high unemployment, the introduction of exchange controls and social unrest have resulted in moderate disruptions in production and distribution, higher production costs and declining profitability for Coca-Cola FEMSA. In Brazil, presidential elections were held in 2006 and incumbent president Luiz Inacio Lula da Silva was reelected for a new four-year term. Although political and economic stability and country risk have improved significantly in Brazil, and currency has strengthened accordingly, we cannot assure you that these positive trends will continue in future periods.

Our future results may be significantly affected by the general economic and financial conditions in the countries where we operate, by the devaluation of the local currency, inflation or interest rates or by political developments or changes in law. Total revenues increased in Coca-Cola FEMSA's non-Mexican territories at a higher rate relative to its Mexican territories in 2006 as compared to prior periods, resulting in a greater contribution to its results of operations from these territories, which also have a lower operating margin. Devaluation of the local currencies against the U.S. dollar may increase our operating costs in these countries, and depreciation against the Mexican peso may negatively affect the results of operations for these countries as reported in our Mexican Financial Reporting Standards financial statements. In addition, some of these countries may impose exchange controls that could impact our ability to purchase raw materials in foreign currencies and the ability of the subsidiaries in these countries to remit dividends abroad or make payments other than in local currencies, as is currently the case in Venezuela under regulations imposed in January 2003 that continue to apply. As a result of these potential risks, we may experience lower demand, lower real pricing or increases in costs, which may negatively impact our results of operations.

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### **ITEM 4. INFORMATION ON THE COMPANY**

#### **The Company**

##### **Overview**

We are a Mexican company headquartered in Monterrey, Mexico, and our origin dates back to 1890. Our company was incorporated on May 30, 1936 and has a duration of 99 years. Our legal name is Fomento Económico Mexicano, S.A.B. de C.V., and in commercial contexts we frequently refer to ourselves as FEMSA. On December 5, 2006, as required by the new Mexican Securities Law, we changed our name to reflect that we are a *sociedad anónima bursátil de capital variable* (a variable capital listed stock corporation), whereas previously companies' names in Mexico, including ours, did not indicate whether the company was a listed company (*sociedad anónima de capital variable*). Our principal executive offices are located at General Anaya No. 601 Pte., Colonia Bella Vista, Monterrey, Nuevo León 64410, Mexico. Our telephone number at this location is (52-81) 8328-6000. Our website is [www.femsa.com](http://www.femsa.com). We are organized as a *sociedad anónima bursátil de capital variable* under the laws of Mexico. Our agent in the U.S. is Donald Puglisi, 850 Library Avenue, Suite 204, P.O. Box 885, Newark, Delaware 19715.

We conduct our operations through the following principal holding companies, each of which we refer to as a principal sub-holding company:

Coca-Cola FEMSA, which engages in the production, distribution and marketing of soft drinks;

FEMSA Cerveza, which engages in the production, distribution and marketing of beer; and

FEMSA Comercio, which operates convenience stores.

#### **Corporate Background**

FEMSA traces its origins to the establishment of Mexico's first brewery, Cervecería Cuauhtémoc, S.A. de C.V., which we refer to as Cuauhtémoc, that was founded in 1890 by four Monterrey businessmen: Francisco G. Sada, José A. Muguerza, Isaac Garza and José M. Schneider. Descendants of certain of the founders of Cuauhtémoc control our company.

In 1891, the first year of production, Cuauhtémoc produced 2,000 hectoliters of beer. Cuauhtémoc continued to expand through additions to existing plant capacity and through acquisitions of other Mexican breweries, and has continued to increase its production capacity, reaching approximately 33.696 million hectoliters in 2006.

The strategic integration of our company dates back to 1936 when our packaging operations were established to supply crown caps to the brewery. The packaging operations were expanded in 1957 when we began to produce labels and flexible packaging. During this period, these operations were part of what was known as the Monterrey Group, which also included interests in banking, steel and other packaging operations.

In 1974, the Monterrey Group was split between two branches of the descendants of the founding families of Cuauhtémoc. The steel and other packaging operations formed the basis for the creation of Corporación Siderúrgica, S.A. (later Alfa, S.A.B. de C.V.), controlled by the Garza Sada family, and the beverage and banking operations were consolidated under the FEMSA corporate umbrella, controlled by the Garza Lagüera family. FEMSA's shares were first listed on the Mexican Stock Exchange on September 19, 1978. Between 1977 and 1981, FEMSA diversified its operations through acquisitions in the soft drinks and mineral water industries, the establishment of the first convenience stores under the trade name Oxxo and other investments in the hotel, construction, auto parts, food and fishing industries, which were considered non-core businesses and were subsequently divested.

In August 1982, the Mexican government suspended payment on its international debt obligations and nationalized the Mexican banking system. In 1985, certain controlling shareholders of FEMSA acquired a controlling interest in Cervecería Moctezuma, S.A., which was then Mexico's third-largest brewery and which we refer to as Moctezuma, and related companies in the packaging industry. FEMSA subsequently undertook an extensive corporate and financial restructuring that was completed in December 1988.





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Pursuant to the 1988 restructuring, FEMSA's assets were combined under a single corporate entity, which became Grupo Industrial Emprex, S.A. de C.V., which we refer to as Emprex. The debt restructuring included a capital increase, capitalization of debt and a divestiture of interests in non-core businesses. As a result of these transactions, FEMSA's interest in Emprex was diluted to 60%, only to increase subsequently to approximately 68% as a result of the exercise of certain option rights by FEMSA.

In August 1991, FEMSA repurchased approximately 30% of its shares from a dissident minority shareholder. In October 1991, certain majority shareholders of FEMSA acquired a controlling interest in Bancomer, S.A., which we refer to as Bancomer. The investment in Bancomer was undertaken as part of the Mexican government's reprivatization of the banking system, which had been nationalized in 1982. The Bancomer acquisition was financed in part by a subscription by Emprex's shareholders, including FEMSA, of shares in Grupo Financiero Bancomer, S.A. de C.V. (currently Grupo Financiero BBVA Bancomer, S.A. de C.V.), which we refer to as BBVA Bancomer, the Mexican financial services holding company that was formed to hold a controlling interest in Bancomer. In February 1992, FEMSA offered Emprex's shareholders the opportunity to exchange the BBVA Bancomer shares to which they were entitled for Emprex shares owned by FEMSA. As a result, FEMSA's interest in Emprex declined to approximately 62%. In connection with these transactions, an 11% interest in Emprex was issued to a European portfolio investor. This reduced FEMSA's interest in Emprex to approximately 51%. In August 1996, the shares of BBVA Bancomer that were received by FEMSA in the exchange with Emprex's shareholders were distributed as a dividend to FEMSA's shareholders.

Upon the completion of these transactions, Emprex began a series of strategic transactions to strengthen the competitive positions of its operating subsidiaries. These transactions included the sale of a 30% strategic interest in Coca-Cola FEMSA to a wholly-owned subsidiary of The Coca-Cola Company and a subsequent public offering of Coca-Cola FEMSA shares, both of which occurred in 1993, and the sale of a 22% strategic interest in FEMSA Cerveza to Labatt Brewing Company Limited, which we refer to as Labatt, in 1994. Labatt, which was later acquired by InBev S.A., or InBev (known at the time of the acquisition of Labatt as Interbrew), subsequently increased its interest in FEMSA Cerveza to 30%.

In 1998, we completed a reorganization that:

simplified our capital structure by converting our outstanding capital stock at the time of the reorganization into BD Units and B Units, and

united the shareholders of FEMSA and the former shareholders of Emprex at the same corporate level through an exchange offer that was consummated on May 11, 1998.

As part of the reorganization, FEMSA listed ADSs on the New York Stock Exchange representing BD Units, and listed the BD Units and its B Units on the Mexican Stock Exchange. Prior to the completion of the exchange offer, FEMSA owned 51.04% of the shares of Emprex. Upon the completion of the exchange offer, FEMSA owned 98.70% of the outstanding shares of Emprex, which amount increased to 99.99% through a tender offer by FEMSA for the remaining Emprex shares.

In July 2002, as a result of the split-up or *escisión* of Emprex, Compañía Internacional de Bebidas, S.A. de C.V., which we refer to as CIBSA, was created as a new company to hold our interest in Coca-Cola FEMSA.

In May 2003, our subsidiary Coca-Cola FEMSA expanded its operations throughout Latin America by acquiring 100% of Panamco, then the largest soft drink bottler in Latin America in terms of sales volume in 2002. Through its acquisition of Panamco, Coca-Cola FEMSA began producing and distributing Coca-Cola trademark beverages in additional territories in Mexico, Central America, Colombia, Venezuela and Brazil, along with bottled water, beer and other beverages in some of these territories. The Coca-Cola Company and its subsidiaries received Series D Shares in exchange for their equity interest in Panamco of approximately 25%.

On August 31, 2004, we consummated a series of transactions with InBev, Labatt and certain of their affiliates to terminate the existing arrangements between FEMSA Cerveza and Labatt. As a result of these transactions, FEMSA acquired 100% ownership of FEMSA Cerveza and previously existing arrangements among affiliates of FEMSA and InBev relating to governance, transfer of ownership and other matters with respect to

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FEMSA Cerveza were terminated. We paid InBev a total of US\$ 1,245 million for its affiliates' 30% interest in FEMSA Cerveza. Pursuant to agreements entered into on June 21, 2004, Heineken USA replaced Labatt USA LLC and Latrobe Brewing Company LLC, which we refer to collectively as Labatt USA, as the exclusive importer, marketer and distributor of FEMSA Cerveza's beer brands in the United States starting on January 1, 2005. On June 1, 2005, we consummated an equity offering of 80.5 million BD Units (including BD Units in the form of ADSs) and 52.78 million B units that resulted in net proceeds to us of US\$ 700 million after underwriting spreads and commissions. We used the proceeds of the equity offering to refinance indebtedness incurred in connection with the transactions with InBev, Labatt and certain of their affiliates.

On January 13, 2006, FEMSA Cerveza acquired 68% of the equity of the Brazilian brewer Kaiser from the Molson Coors Brewing Company, or Molson Coors. FEMSA Cerveza paid US\$ 68 million to Molson Coors to acquire 68% of Kaiser at closing. As part of the transaction to acquire Kaiser, FEMSA Cerveza received certain indemnity provisions from Molson Coors in respect of Kaiser's existing financial debt of approximately US\$ 60 million and other contingent liabilities and claims. Following this transaction, Molson Coors retained a 15% ownership stake in Kaiser, while Heineken N.V.'s previous ownership of 17% remained unchanged. In December 2006, Molson Coors completed its exit from Kaiser by exercising a put option for its 15% holding, pursuant to a right granted to it by FEMSA Cerveza at the time FEMSA Cerveza acquired Kaiser from Molson Coors in January 2006. On December 22, 2006, FEMSA Cerveza completed a capital increase of US\$200 million in Kaiser, following the successful settlement of the contingent liabilities and claims in respect of Kaiser. Heineken N.V. elected not to participate in the increase, thereby diluting its 17% interest in Kaiser to 0.17%. As a result of these transactions, FEMSA Cerveza now holds a 99.83% participation in Kaiser.

On November 3, 2006, we acquired from certain subsidiaries of The Coca-Cola Company 148,000,000 Series D Shares of Coca-Cola FEMSA through our subsidiary CIBSA, representing 8.02% of the total outstanding stock of Coca-Cola FEMSA. We acquired these shares at a price of US\$ 2.888 per share, or US\$ 427.4 million in the aggregate, pursuant to a Memorandum of Understanding with The Coca-Cola Company. As of May 31, 2007, FEMSA indirectly owns 53.7% of the capital stock of Coca-Cola FEMSA (63.0% of its capital stock with full voting rights) and The Coca-Cola Company indirectly owns 31.6% of the capital stock of Coca-Cola FEMSA (37.0% of its capital stock with full voting rights). The remaining 14.7% of its capital consists of Series L Shares with limited voting rights, which trade on the Mexican Stock Exchange and on the New York Stock Exchange in the form of ADSs under the trading symbol KOF.

In December 2006, Coca-Cola FEMSA and The Coca-Cola Company agreed to acquire Jugos del Valle from its controlling shareholders through a 100% tender offer for an aggregate price of US\$ 470 million, including the assumption of net existing debt of approximately US\$ 90 million and subject to net capital and debt adjustments at closing. Upon closing of the transaction, Coca-Cola FEMSA and The Coca-Cola Company would jointly become the second largest juice producer in Mexico and the largest in Brazil, providing a platform for growth in the key non-carbonated beverages segment, which we would expect to outgrow all other beverage categories. If the acquisition closes, the remainder of the Coca-Cola bottler system in Mexico and Brazil would be invited to participate in the Jugos del Valle joint venture in their respective countries of operation under the same economic terms and conditions pursuant to which Coca-Cola FEMSA and The Coca-Cola Company entered into the transaction.

On June 25, 2007, the *Comisión Federal de Competencia* (CFC), or the Mexican Antitrust Commission, notified us of its decision to object to the acquisition of Jugos del Valle. We intend to consider our options with respect to the transaction, which may include seeking a reconsideration of the decision.

On March 7, 2007, Coca-Cola FEMSA issued Ps. 3,000 million in 5-year maturity bonds (*certificados bursátiles*), in part to finance the Jugos del Valle acquisition and in part to refinance certain bond maturities coming due in April 2007.

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**Ownership Structure**

We conduct our business through our principal sub-holding companies as shown in the following diagram and table:

**Principal Sub-holding Companies Ownership Structure**

**As of May 31, 2007**

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<sup>(1)</sup> Percentage of capital stock, equal to 63.0% of capital stock with full voting rights.

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The following tables present an overview of our operations by reportable segment and by geographic region under Mexican Financial Reporting Standards:

**Operations by Segment Overview****Year Ended December 31, 2006<sup>(1)(2)</sup>**

	Coca-Cola FEMSA		FEMSA Cerveza		FEMSA Comercio	
	(in millions of constant Mexican pesos,					
	except for employees and percentages)					
Total revenues	Ps. 57,738	44.8%	Ps. 35,599	27.6%	Ps. 35,500	27.6%
Income from operations	9,456	54.4	5,915	34.0	1,604	9.2
Total assets	75,024	51.6	58,588	40.2	11,865	8.2
Employees	56,682	58.0%	23,201	23.7%	11,452	11.7%

**Total Revenues Summary by Segment<sup>(1)</sup>**

	Year Ended December 31,		
	2006	2005	2004
	(in millions of constant Mexican pesos)		
Coca-Cola FEMSA	Ps. 57,738	Ps. 53,997	Ps. 51,276
FEMSA Cerveza	35,599	28,690	26,848
FEMSA Comercio	35,500	29,898	24,556
Other	7,678	6,250	5,610
Consolidated total revenues	Ps. 126,427	Ps. 111,636	Ps. 102,316

**Total Revenues Summary by Geographic Region<sup>(3)</sup>**

	Year Ended December 31,		
	2006	2005	2004
	(in millions of constant Mexican pesos)		
Mexico	Ps. 95,795	Ps. 87,281	Ps. 79,634
Central America	4,145	3,636	3,736
Colombia	5,586	5,238	4,734
Venezuela	6,536	5,875	5,563
Brazil	11,340	6,650	5,865
Argentina	3,281	3,090	2,871
Consolidated total revenues	Ps. 126,427	Ps. 111,636	Ps. 102,316

- (1) The sum of the financial data for each of our segments and percentages with respect thereto differ from our consolidated financial information due to intercompany transactions, which are eliminated in consolidation, and certain assets and activities of FEMSA.
- (2) Excludes our other business segment, which had total revenues of Ps. 7,678 million and income from operations of Ps. 415 million in 2006.
- (3) The sum of the financial data for each geographic region differs from our consolidated financial information due to intercompany transactions, which are eliminated in consolidation.



**Table of Contents****Significant Subsidiaries**

The following table sets forth our significant subsidiaries as of May 31, 2007:

<b>Name of Company</b>	<b>Jurisdiction of Establishment</b>	<b>Percentage Owned</b>
<b>CIBSA</b>	Mexico	100.0%
<b>Coca-Cola FEMSA</b>	Mexico	53.7 <sup>(1)</sup>
Propimex, S.A. de C.V.	Mexico	53.7
Corporación Interamericana de Bebidas, S.A. de C.V. (Panamco)	Mexico	53.7
Panamco México, S.A. de C.V.	Mexico	53.3
Industria Nacional de Gaseosas, S.A. (holding company of Colombian operations).	Colombia	52.5
Kristine Overseas, S.A. de C.V. (holding company of Brazilian operations)	Mexico	44.6
<b>Emprex Cerveza, S.A. de C.V. (Emprex Cerveza)</b>	Mexico	100.0
<b>FEMSA Cerveza</b>	Mexico	100.0
Cervecería Cuauhtémoc Moctezuma, S.A. de C.V.	Mexico	100.0
Cervezas Cuauhtémoc Moctezuma, S.A. de C.V.	Mexico	100.0
<b>Emprex</b>	Mexico	100.0
<b>FEMSA Comercio</b>	Mexico	100.0
Cadena Comercial Oxxo, S.A. de C.V.	Mexico	100.0
Oxxo Express, S.A. de C.V.	Mexico	100.0

(1) Percentage of capital stock. FEMSA owns 63.0% of the capital stock with full voting rights.

**Business Strategy**

We are a beverage company. Our soft drink operation, Coca-Cola FEMSA, is the largest bottler of Coca-Cola products in Latin America and the second largest in the world, measured in terms of sales volumes in 2006, and our brewing operation, FEMSA Cerveza, is both a significant competitor in the Mexican and Brazilian beer markets as well as an exporter in key international markets including the United States. Coca-Cola FEMSA and FEMSA Cerveza are our core businesses, which together define our identity and represent the avenues for our future growth. Our beverage businesses are enhanced by Oxxo, the largest convenience store chain in Mexico measured in terms of number of stores at December 31, 2006 and a significant growth driver in its own right.

As a beverage company, we understand the importance of connecting with our end consumers by interpreting their needs, and ultimately delivering the right products to them for the right occasions. We strive to achieve this by developing the value of our brands, expanding our significant distribution capabilities, including aligning our interests with those at our third-party distribution partners in the beer market in Mexico, which in some instances involve us acquiring these third-party partners, and improving the efficiency of our operations. We continue to improve our information gathering and processing systems in order to better know and understand what our consumers want and need, and we are improving our production and distribution by more efficiently leveraging our asset base.

We believe that the competencies that our businesses have developed can be replicated in other geographic regions. This underlying principle guided our consolidation efforts, which culminated in Coca-Cola FEMSA's acquisition of Panamco on May 6, 2003. The continental platform that this new combination produces encompassing a significant territorial expanse in Mexico and Central America, including some of the most populous metropolitan areas in Latin America we believe may provide us with opportunities to create value through both an improved ability to execute our strategies and the use of superior marketing tools.

Our ultimate objectives are achieving sustainable revenue growth, improving profitability and increasing the return on invested capital in each of our operations. We believe that by achieving these goals we will create sustainable value for our shareholders.

**Table of Contents****Coca-Cola FEMSA****Overview and Background**

Coca-Cola FEMSA is the largest bottler of *Coca-Cola* trademark beverages in Latin America, and the second largest in the world, calculated in each case by sales volume in 2006. It operates in the following territories:

Mexico a substantial portion of central Mexico (including Mexico City) and southeast Mexico (including the Gulf region).

Central America Guatemala (Guatemala City and surrounding areas), Nicaragua (nationwide), Costa Rica (nationwide) and Panama (nationwide).

Colombia most of the country.

Venezuela nationwide.

Argentina Buenos Aires and surrounding areas.

Brazil the area of greater São Paulo, Campinas, Santos, the state of Mato Grosso do Sul and part of the state of Goiás.

Coca-Cola FEMSA was organized on October 30, 1991 as a *sociedad anónima de capital variable* (a variable capital stock corporation) under the laws of Mexico with a duration of 99 years. On December 5, 2006, in response to the Mexican Securities Law, it became a *sociedad anónima bursátil de capital variable* (a variable capital listed stock corporation). Its principal executive offices are located at Guillermo González Camarena No. 600, Col. Centro de Ciudad Santa Fé, Delegación Álvaro Obregón, México, D.F., 01210, México. Coca-Cola FEMSA's telephone number at this location is (52-55) 5081-5100. Its website is [www.coca-colafemsa.com](http://www.coca-colafemsa.com).

The following is an overview of Coca-Cola FEMSA's operations by geographic region in 2006:

**Operations by Geographic Region Overview****Year Ended December 31, 2006<sup>(1)</sup>**

	<b>Total Revenues</b>	<b>Percentage of Total Revenues</b>	<b>Income from Operations</b>	<b>Percentage of Income from Operations</b>
Mexico	Ps. 30,360	52.6	Ps. 6,390	67.6
Central America	4,142	7.2	613	6.5
Colombia	5,507	9.5	727	7.7
Venezuela	6,532	11.3	169	1.8
Argentina	3,281	5.7	419	4.4
Brazil	7,916	13.7	1,138	12.0

<sup>(1)</sup> Expressed in millions of Mexican pesos, except for percentages.

**Corporate History**



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In 1979, one of our subsidiaries acquired certain soft drink bottlers that are now a part of Coca-Cola FEMSA. At that time, the acquired bottlers had 13 Mexican distribution centers operating 701 distribution routes, and their production capacity was 83 million physical cases. In 1991, we transferred our ownership in the bottlers to FEMSA Refrescos, S.A. de C.V., the corporate predecessor to Coca-Cola FEMSA, S.A.B. de C.V.

In June 1993, a subsidiary of The Coca-Cola Company subscribed for 30% of Coca-Cola FEMSA's capital stock in the form of Series D Shares for US\$ 195 million. In September 1993, we sold Series L Shares that represented 19% of Coca-Cola FEMSA's capital stock to the public, and Coca-Cola FEMSA listed these shares on the Mexican Stock Exchange and, in the form of ADSs, on the New York Stock Exchange.

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In a series of transactions between 1994 and 1997, Coca-Cola FEMSA acquired the territory for its operations in Buenos Aires, Argentina from a subsidiary of The Coca-Cola Company. Coca-Cola FEMSA expanded its Argentine operations in February 1996 by acquiring territories for the contiguous San Isidro and Pilar areas.

Coca-Cola FEMSA expanded its Mexican operations in November 1997 by acquiring a territory in the state of Chiapas in southern Mexico, after which it covered the entire state of Chiapas.

In May 2003, it acquired Panamco and began producing and distributing *Coca-Cola* trademark beverages in additional territories in the central and the gulf regions of Mexico and in Central America (Guatemala, Nicaragua, Costa Rica and Panama), Colombia, Venezuela and Brazil, along with bottled water, beer and other beverages in some of these territories. As a result of the acquisition, the interest of The Coca-Cola Company in the capital stock of Coca-Cola FEMSA increased from 30% to 39.6%.

During August 2004, Coca-Cola FEMSA conducted a rights offering to allow existing holders of its Series L Shares and ADSs to acquire newly-issued Series L Shares in the form of Series L Shares and ADSs, respectively. The purpose of the rights offering was to permit holders of Series L Shares, including in the form of ADSs, to subscribe on a proportionate basis at the same price per share at which FEMSA and The Coca-Cola Company subscribed in connection with the Panamco acquisition. The rights offering expired on September 1, 2004. On March 8, 2006, Coca-Cola FEMSA's shareholders approved the non-cancellation of the 98,684,857 Series L Shares (equivalent to approximately 9.87 million ADSs) that were not subscribed for in the rights offering. These shares are available for issuance in connection with future transactions and on terms and conditions determined by Coca-Cola FEMSA's board of directors at an issuance price of no less than US\$ 2.216 per share or its equivalent in Mexican currency.

On November 3, 2006, we acquired, through a subsidiary, 148,000,000 of Coca-Cola FEMSA's Series D Shares from certain subsidiaries of The Coca-Cola Company representing 9.4% of the total outstanding voting shares and 8.0% of the total outstanding equity of Coca-Cola FEMSA, at a price of US\$ 2.888 per share for an aggregate amount of US\$ 427.4 million. The acquisition of such additional shares took place pursuant to the Memorandum of Understanding between FEMSA and The Coca-Cola Company relating to the acquisition of Panamco by Coca-Cola FEMSA in 2003. See Item 7. Major Shareholders and Related Party Transactions Major Shareholders The Coca-Cola Memorandum. With this purchase, we increased our ownership to 53.7% of Coca-Cola FEMSA's capital stock. Pursuant to Coca-Cola FEMSA's bylaws, the acquired shares were converted from Series D Shares to Series A Shares.

On December 19, 2006, Coca-Cola FEMSA and The Coca-Cola Company announced an agreement with the controlling shareholders of Jugos del Valle to conduct a public tender offer in Mexico of up to 100% of the outstanding public shares of Jugos del Valle for approximately US\$380 million in cash. The price assumes a total aggregate value of US\$470 million and that Jugos del Valle has approximately US\$90 million in net debt. The final price to be paid would be based on the actual level of debt, net working capital and other liabilities on the date the tender offer is launched. The tender offer would be launched once applicable regulatory approvals were obtained. Coca-Cola FEMSA anticipates that, if the transaction closes, other bottlers in Mexico and Brazil would be invited to participate subsequent to the completion of the acquisition on the same basic terms and conditions.

On June 25, 2007 the *Comisión Federal de Competencia* of Mexico (CFC), or the Mexican Antitrust Commission, notified us of its decision to object to the acquisition of Jugos del Valle. We intend to consider our options with respect to the transaction, which may include seeking a reconsideration of the decision.

Jugos del Valle is the second largest producer of packaged juices, nectars and fruit flavored beverages in Mexico, the largest producer in Brazil of such products, and it has a presence in other Latin American markets. Jugos del Valle generated approximately US\$440 million in total revenues for the 12-month period ended September 30, 2006. If consummated, the transaction would greatly increase Coca-Cola FEMSA's and The Coca-Cola Company's presence in the non-carbonated beverage segment in Latin America. The transaction is subject to certain conditions, including applicable regulatory approvals, which were not granted upon initial review by the CFC.

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As of March 31, 2007, we indirectly owned Series A Shares equal to 53.7% of Coca-Cola FEMSA's capital stock (63.0% of Coca-Cola FEMSA's capital stock with full voting rights), and The Coca-Cola Company indirectly owned Series D Shares equal to 31.6% of the capital stock of Coca-Cola FEMSA (37.0% of Coca-Cola FEMSA's capital stock with full voting rights). Series L Shares with limited voting rights, which trade on the Mexican Stock Exchange and in the form of ADSs on the New York Stock Exchange, constitute the remaining 14.7% of Coca-Cola FEMSA's capital stock.

## **Business Strategy**

Coca-Cola FEMSA is the largest bottler of *Coca-Cola* trademark beverages in Latin America in terms of total sales volume in 2006, with operations in Mexico, Guatemala, Nicaragua, Costa Rica, Panama, Colombia, Venezuela, Argentina and Brazil. While Coca-Cola FEMSA's corporate headquarters are in Mexico City, it has established divisional headquarters in the following three regions:

Mexico with headquarters in Mexico City;

Latin Centro (covering territories in Guatemala, Nicaragua, Costa Rica, Panama, Colombia and Venezuela) with headquarters in San José, Costa Rica; and

Mercosur (covering territories in Argentina and Brazil) with headquarters in São Paulo, Brazil.

Coca-Cola FEMSA seeks to provide its shareholders with an attractive return on their investment by increasing its profitability. The key factors in achieving profitability are increasing its revenues by (1) implementing multi-segmentation strategies in its major markets to target distinct market clusters divided by competitive intensity and socioeconomic levels; (2) implementing well-planned product, packaging and pricing strategies through channel distribution; and (3) achieving operational efficiencies throughout Coca-Cola FEMSA. To achieve these goals Coca-Cola FEMSA continues its efforts in:

working with The Coca-Cola Company to develop a business model to continue exploring new lines of beverages, extend existing products, participate in new beverage segments and effectively advertise and market its products;

developing and expanding its non-carbonated beverage portfolio organically and through strategic acquisitions together with The Coca-Cola Company;

implementing packaging strategies designed to increase consumer demand for its products and to build a strong returnable base for the Coca-Cola brand selectively;

replicating its successful best practices throughout the whole value chain;

rationalizing and adapting its organizational and asset structure in order to be in a better position to respond to a changing competitive environment;

strengthening its selling capabilities and selectively implementing its pre-sale system, in order to get closer to its clients and help them satisfy the beverage needs of consumers;

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evaluating its bottled water strategy, in conjunction with The Coca-Cola Company, to maximize its profitability across its market territories;

committing to building a strong collaborative team, from top to bottom; and

seeking to expand its geographical footprint.

Coca-Cola FEMSA seeks to increase per capita consumption of soft drinks in the territories in which it operates. To that end, its marketing teams continuously develop sales strategies tailored to the different characteristics of its various territories and channels. Coca-Cola FEMSA continues to develop its product portfolio to better meet market demand and maintain its overall profitability. To stimulate and respond to consumer demand, it continues to introduce new products and new presentations. See **Product and Packaging Mix**. It also seeks to increase placement of refrigeration equipment, including promotional displays, through the

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strategic placement of such equipment in retail outlets in order to showcase and promote its products. In addition, because Coca-Cola FEMSA views its relationship with The Coca-Cola Company as integral to its business strategy, it uses market information systems and strategies developed with The Coca-Cola Company to improve its coordination with the worldwide marketing efforts of The Coca-Cola Company. See Marketing Channel Marketing.

Coca-Cola FEMSA seeks to rationalize its manufacturing and distribution capacity to improve the efficiency of its operations. In 2003 and 2004, as part of the integration process from its acquisition of Panamco, it closed several under-utilized manufacturing centers and shifted distribution activities to other existing facilities. Coca-Cola FEMSA closed additional distribution centers in 2005 and 2006. See Description of Property, Plant and Equipment. In each of its facilities, Coca-Cola FEMSA seeks to increase productivity through infrastructure and process reengineering for improved asset utilization. Its capital expenditure program includes investments in production and distribution facilities, bottles, cases, coolers and information systems. Coca-Cola FEMSA believes that this program will allow it to maintain its capacity and flexibility to innovate and to respond to consumer demand for non-alcoholic beverages.

Finally, Coca-Cola FEMSA focuses on management quality as a key element of its growth strategies and remains committed to fostering the development of quality management at all levels. Both our company and The Coca-Cola Company provide Coca-Cola FEMSA with managerial experience. To build upon these skills, Coca-Cola FEMSA also offers management training programs designed to enhance its executives abilities, exchange experiences, know-how and talent among an increasing number of multinational executives from its new and existing territories.

### **Coca-Cola FEMSA's Markets**

The following map shows the locations of Coca-Cola FEMSA's territories, giving estimates in each case of the population to which it offers products, the number of retailers of its carbonated soft drinks and the per capita consumption of its carbonated soft drinks:

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Per capita consumption data for a territory is determined by dividing carbonated soft drink sales volume within the territory (in bottles, cans, and fountain containers) by the estimated population within such territory, and is expressed on the basis of the number of eight-ounce servings of Coca-Cola FEMSA's products consumed annually per capita. In evaluating the development of local volume sales in its territories, Coca-Cola FEMSA and The Coca-Cola Company measure, among other factors, the per capita consumption of Coca-Cola FEMSA's carbonated soft-drinks.

**Coca-Cola FEMSA's Products**

Coca-Cola FEMSA produces, markets and distributes *Coca-Cola* trademark beverages, proprietary brands and brands licensed from third parties. The *Coca-Cola* trademark beverages include colas, flavored soft drinks, water and beverages in other categories such as juice drinks and isotonics. The following table sets forth Coca-Cola FEMSA's main brands as of March 31, 2007:

	<b>Central</b>					
<i>Colas:</i>	<b>Mexico</b>	<b>America</b>	<b>Colombia</b>	<b>Venezuela</b>	<b>Brazil</b>	<b>Argentina</b>
<i>Coca-Cola</i>	ü	ü	ü	ü	ü	ü
<i>Coca-Cola light</i>	ü	ü	ü	ü	ü	ü

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	Central					
<i>Flavored Soft Drinks:</i>	Mexico	America	Colombia	Venezuela	Brazil	Argentina
<i>Chinotto</i>				ü		
<i>Crush</i>			ü			ü
<i>Fanta</i>	ü	ü	ü		ü	ü
<i>Fresca</i>	ü					
<i>Frescolita</i>		ü		ü		
<i>Hit</i>				ü		
<i>Kuat</i>					ü	
<i>Lift</i>	ü	ü	ü			
<i>Mundet<sup>(1)</sup></i>	ü					
<i>Premio<sup>(2)</sup></i>			ü			
<i>Quatro</i>			ü			ü
<i>Simba</i>					ü	
<i>Sprite</i>	ü	ü	ü		ü	ü
<i>Taí</i>					ü	ü

	Mexico	Central America	Colombia	Venezuela	Brazil	Argentina
<i>Water:</i>		ü				
<i>Alpina<sup>(2)</sup></i>		ü				
<i>Ciel</i>	ü					
<i>Crystal<sup>(2)</sup></i>					ü	
<i>Manantial</i>			ü			
<i>Nevada</i>				ü		
<i>Santa Clara<sup>(2)</sup></i>			ü			

	Mexico	Central America	Colombia	Venezuela	Brazil	Argentina
<i>Other Categories:</i>		ü				
<i>Dasani<sup>(3)</sup></i>		ü	ü			ü
<i>Hi-C<sup>(4)</sup></i>		ü				ü
<i>Nestea</i>	ü	ü		ü	ü	
<i>Powerade<sup>(5)</sup></i>	ü	ü	ü	ü		
<i>Sonfil<sup>(4)</sup></i>				ü		

(1) Brand licensed from FEMSA.

(2) Proprietary brand.

(3) Flavored no-calorie water. (In Argentina also as still water)

(4) Juice based drink.

(5) Isotonic.

**Sales Overview**

Coca-Cola FEMSA measures total sales volume in terms of unit cases. Unit case refers to 192 ounces of finished beverage product (24 eight-ounce servings) and, when applied to fountain syrup, powders and concentrate, refers to the volume of fountain syrup, powders and concentrate that is required to produce 192 ounces of finished beverage product. The following table illustrates Coca-Cola FEMSA's historical sales volume for each of its territories.

	<b>Sales Volume</b>		
	<b>Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
	<b>(millions of unit cases)</b>		
Mexico	1,070.7	1,025.0	989.9
Central America	120.3	109.4	110.6
Colombia	190.9	179.7	167.1
Venezuela	182.6	172.5	172.7
Argentina	164.9	150.1	144.3
Brazil	268.7	252.5	227.5
<b>Combined Volume</b>	<b>1,998.1</b>	<b>1,889.2</b>	<b>1,812.1</b>



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### **Product and Packaging Mix**

Coca-Cola FEMSA's most important brand is *Coca-Cola* and its line extensions, *Coca-Cola light*, *Coca-Cola light caffeine free* and *Coca-Cola light with lime*, which together accounted for 62.5% of total sales volume in 2006. *Ciel* (including jug presentations), *Fanta*, *Sprite*, *Lift* and *Fresca*, Coca-Cola FEMSA's next largest brands in consecutive order, accounted for 10.5%, 6.1%, 3.0%, 1.9% and 1.7%, respectively, of total sales volume in 2006. Coca-Cola FEMSA uses the term line extensions to refer to the different flavors in which it offers its brands. Coca-Cola FEMSA produces, markets and distributes *Coca-Cola* trademark beverages in each of its territories in containers authorized by The Coca-Cola Company, which consist of a variety of returnable and non-returnable presentations in the form of glass bottles, cans and plastic bottles made of polyethylene terephthalate, which it refers to as PET.

Coca-Cola FEMSA uses the term presentation to refer to the packaging unit in which it sells its products. Presentation sizes for our *Coca-Cola* trademark beverages range from a 4-ounce personal size to a 20-liter multiple serving size. Coca-Cola FEMSA considers a multiple serving size as equal to or larger than 1.0 liter. In general, personal sizes have a higher price per unit case as compared to multiple serving sizes. Coca-Cola FEMSA offers both returnable and non-returnable presentations, which allows it to offer different combinations of convenience and price to implement revenue management strategies and to target specific distribution channels and population segments in its territories. In addition, it sells some *Coca-Cola* trademark beverage syrups in containers designed for soda fountain use, which it refers to as fountain. Coca-Cola FEMSA also sells bottled water products in jug sizes, which refers to sizes larger than 17 liters, that have a much lower price per unit than its other beverage products.

In addition to *Coca-Cola* trademark beverages, Coca-Cola FEMSA produces, markets and distributes certain other proprietary brands and beverages licensed from third parties other than The Coca-Cola Company in a variety of presentations.

Coca-Cola FEMSA's core brands are principally the *Coca-Cola* trademark beverages. It sells certain of these brands or their line extensions at a premium in some of our territories, in which it refers to them as premium brands. Coca-Cola FEMSA also sells certain other brands at a lower price per ounce, which it refers to as value protection brands.

The characteristics of Coca-Cola FEMSA's territories are very diverse. Central Mexico and Coca-Cola FEMSA's territories in Argentina are densely populated and have a large number of competing carbonated soft drink brands as compared to the rest of our territories. Brazil is densely populated but has lower per capita consumption of carbonated soft drink products as compared to Mexico. Portions of Central America and Colombia are large and mountainous areas with lower population density, lower per capita income and lower per capita consumption of soft drink products. In Venezuela, per capita consumption of Coca-Cola FEMSA's products has improved in spite of operating disruptions faced in 2006.

The following discussion analyzes Coca-Cola FEMSA's product and packaging mix by segment. The volume data presented is for the years 2006, 2005 and 2004.

**Mexico.** Coca-Cola FEMSA's product portfolio consists of *Coca-Cola* trademark beverages, and since 2001 has included the *Mundet* trademark beverages. In 2007, as part of its efforts to revitalize the *Coca-Cola* brand Coca-Cola FEMSA launched *Coca-Cola Zero*, a line extension of the *Coca-Cola* brand. Carbonated soft drink per capita consumption of Coca-Cola FEMSA's products in its Mexican territories in 2006 was 410 eight-ounce servings.

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The following table highlights historical sales volume and mix in Mexico for its products:

	Year Ended December 31,		
	2006	2005	2004
(millions of unit cases)			
<b>Product Sales Volume</b>			
Total	1,070.7	1,025.0	989.9
% Growth	4.5%	3.5%	(1.2)%
(in percentages)			
<b>Unit Case Volume Mix by Category</b>			
Total Carbonated Soft Drinks	79.6%	79.6%	80.4%
Water <sup>(1)</sup>	19.5	19.7	19.1
Other Categories	0.9	0.7	0.5
Total	100.0%	100.0%	100.0%
(in percentages)			
<b>Product Mix by Presentation</b>			
Returnable	26.0%	26.6%	28.4%
Non-returnable and fountain	59.2	58.4	57.2
Jug	14.8	15.0	14.4
Total	100.0%	100.0%	100.0%

(1) Includes jug volume.

Coca-Cola FEMSA's most popular soft drink presentations were the 2.5-liter returnable plastic bottle, the 0.6-liter non-returnable plastic bottle and the 2.5-liter non-returnable plastic bottle, which together accounted for 55% of total carbonated soft drink sales volume in Mexico in 2006. Since 2004, Coca-Cola FEMSA has introduced a number of new presentations in Mexico. These include 2.5-liter returnable plastic bottles, 1.25-liter returnable glass bottles, 1.5-liter non-returnable plastic bottles, 8, 10.5 and 16-ounce cans, 0.45-liter non-returnable plastic bottles, 0.71-liter non-returnable plastic bottles and 4-ounce non-returnable glass bottles. During 2006, Coca-Cola FEMSA complemented its portfolio in the returnable presentations with the roll-out of a 1.25-liter returnable glass presentation at an affordable price. This presentation accounted for over 30% of its incremental volume in the year. Multiple serving presentations are an important component of its product mix. In 2006, multiple serving presentations represented 63.4% of total carbonated soft drink sales volume in Mexico, representing 6.8% growth as compared to 2005. Coca-Cola FEMSA's commercial strategies seek to foster consumption in single serving presentations while maintaining multiple serving volumes.

In the past, the packaging trend in the soft drink industry in Mexico had moved toward non-returnable presentations. However, in 2004, due to the entrance of low price brands in multiple serving size presentations, Coca-Cola FEMSA refocused its packaging mix strategy to reinforce its sales of multiple serving size returnable packages. As a result, carbonated soft drink non-returnable presentations remained almost flat as a percentage of total sales volume in Mexico in 2004. In 2006, Coca-Cola FEMSA's carbonated soft drink non-returnable presentations slightly increased as a percentage of its total sales volume from 68.7% in 2005 to 69.5% in 2006. Returnable plastic and glass presentations offer consumers a more affordable, although less convenient, product. Coca-Cola FEMSA believes returnable packages present an opportunity to attract new customers and maintain customer loyalty, because they make *Coca-Cola* trademark beverages more attractive to price-sensitive consumers. The price of a 2.5-liter returnable package is normally more than 14% lower than a non-returnable package of the same size. These returnable products are mainly sold to small store retailers, which represent the largest distribution channel in the Mexican market, and benefit from returnable bottles' lower price per ounce, which allows them to compete with larger supermarkets. Coca-Cola FEMSA believes that its continued commitment to returnable bottle availability will allow it to compete with low-price entrants to the Mexican soft drink market.

Total sales volume reached 1,070.7 million unit cases in 2006, an increase of 4.5% compared to 1,025.0 million unit cases in 2005. Carbonated soft drink sales volume grew 4.4%, accounting for almost 80% of the total incremental volumes during the year. Carbonated soft drink volume growth was mainly driven by strong growth of the *Coca-Cola* brand.



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**Central America.** Coca-Cola FEMSA's product sales in Central America consist predominantly of *Coca-Cola* trademark beverages. In 2006, the per capita consumption of carbonated *Coca-Cola* soft drink products in Central America was 151 eight-ounce servings.

The following table highlights historical total sales volume and sales volume mix in Central America:

	Year Ended December 31,		
	2006	2005	2004
	(millions of unit cases)		
<b>Product Sales Volume</b>			
Total	120.3	109.4	110.6
% Growth	10.0%	(1.1)%	3.1%
	(in percentages)		
<b>Unit Case Volume Mix by Category</b>			
Total Carbonated Soft Drinks	90.9%	93.6%	94.3%
Water	4.4	4.3	4.1
Other Categories	4.7	2.1	1.6
Total	100.0%	100.0%	100.0%
	(in percentages)		
<b>Product Mix by Presentation</b>			
Returnable	34.9%	41.9%	48.3%
Non-returnable and fountain	65.1	58.1	51.7
Jug			
Total	100.0%	100.0%	100.0%

In Central America, Coca-Cola FEMSA sells the majority of its sales volume through small retailers. In 2006, multiple serving presentations represented 50.6% of total carbonated soft drink sales volume in Central America, compared with 48.8% in 2005. Beginning in 2004, Coca-Cola FEMSA faced greater competition as a result of the entrance of low price brands in the Central American region. As a result, Coca-Cola FEMSA reinforced its packaging portfolio offering for the *Coca-Cola* brand with the introduction of 1.5-liter and 2.5-liter non-returnable plastic bottles and a more affordable 2.5-liter returnable plastic bottle. In 2006, looking for a higher participation in the growing non-carbonated beverage segment, Coca-Cola FEMSA complemented its product portfolio with the inclusion of *Hi-C*, a juice based product.

Total sales volume was 120.3 million unit cases in 2006, increasing 10.0% compared to 109.4 million in 2005. Carbonated soft drink volumes in the year accounted for 60% of Coca-Cola FEMSA's total incremental volume and non-carbonated beverages were the majority of the balance.

**Colombia.** Coca-Cola FEMSA's product portfolio in Colombia consists of *Coca-Cola* trademark beverages, certain products sold under proprietary trademarks and other brands, which Coca-Cola FEMSA licenses from third parties. In 2006, the per capita consumption of carbonated *Coca-Cola* soft drink products in Colombia was 87 eight-ounce servings.

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The following table highlights historical total sales volume and sales volume mix in Colombia:

	Year Ended December 31,		
	2006	2005	2004
(millions of unit cases)			
<b>Product Sales Volume</b>			
Total	190.9	179.7	167.1
% Growth	6.2%	7.5%	(2.7)%
(in percentages)			
<b>Unit Case Volume Mix by Category</b>			
Total Carbonated Soft Drinks	87.9%	87.9%	86.4%
Water <sup>(1)</sup>	10.9	11.7	13.2
Other Categories	1.2	0.4	0.4
Total	100.0%	100.0%	100.0%
(in percentages)			
<b>Product Mix by Presentation</b>			
Returnable	43.2%	46.2%	50.7%
Non-returnable and fountain	51.3	47.8	42.9
Jug	5.5	6.0	6.4
Total	100.0%	100.0%	100.0%

(1) Includes jug volume.

The Colombian market is characterized by lower per capita consumption and relatively lower levels of non-returnable presentations compared with the rest of Coca-Cola FEMSA's territories. In 2006, multiple serving presentations represented 52.3% of total carbonated soft drink sales volume in Colombia. At the beginning of 2005, Coca-Cola FEMSA launched *Crush Multiflavors* to enhance its competitive position, foster demand for flavored carbonated soft drink brands and leverage its extended distribution and improved execution capabilities countrywide. In 2006, Coca-Cola FEMSA launched *Dasani*, a no-calorie flavored water to complement its product portfolio.

Total sales volume was 190.9 million unit cases in 2006, an increase of 6.2% compared to 179.7 million in 2005, driven by carbonated soft drinks volume growth, which accounted for almost 90% of total incremental volumes.

**Venezuela.** Coca-Cola FEMSA's product portfolio in Venezuela consists predominantly of *Coca-Cola* trademark beverages. In 2006, the per capita consumption of carbonated *Coca-Cola* soft drink products in Venezuela was 147 eight-ounce servings.

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The following table highlights historical total sales volume and sales volume mix in Venezuela:

	Year Ended December 31,		
	2006	2005	2004
	(millions of unit cases)		
<b>Product Sales Volume</b>			
Total	182.6	172.5	172.7
% Growth	5.9%	(0.1)%	13.9%

	(in percentages)		
<b>Unit Case Volume Mix by Category</b>			
Total Carbonated Soft Drinks	87.7%	86.6%	86.3%
Water <sup>(1)</sup>	7.5	8.7	8.2
Other Categories	4.8	4.7	5.5
Total	100.0%	100.0%	100.0%

	(in percentages)		
<b>Product Mix by Presentation</b>			
Returnable	17.5%	24.7%	30.1%
Non-returnable and fountain	81.2	72.2	66.4
Jug	1.3	3.1	3.5
Total	100.0%	100.0%	100.0%

(1) Includes jug volume.

During 2006, Coca-Cola FEMSA continued facing periodic operating difficulties that prevented it from producing and distributing enough supply. Coca-Cola FEMSA implemented a product portfolio rationalization strategy in the second half of the year, which enabled it to increase its total sales volume for the year by 5.9%.

In 2006, multiple serving presentations represented 69.1% of total carbonated soft drink sales volume in Venezuela. Total sales volume was 182.6 million unit cases in 2006, an increase of 5.9% compared to 172.5 million in 2005, driven by volume growth in the carbonated soft drink segment. In 2006, Coca-Cola FEMSA focused on fostering volume growth of its core flavored carbonated soft drinks, posting a 13% growth for the year in this category. These incremental volumes, combined with volume growth of the *Coca-Cola* brand, more than offset volume decline of the value protection brands.

**Argentina.** Coca-Cola FEMSA's product portfolio in Argentina consists exclusively of *Coca-Cola* trademark beverages. In 2006, the per capita consumption of carbonated *Coca-Cola* soft drink products was 351 eight-ounce servings.

The following table highlights historical total sales volume and sales volume mix in Argentina:

	Year Ended December 31,		
	2006	2005	2004
	(millions of unit cases)		
<b>Product Sales Volume</b>			
Total	164.9	150.1	144.3

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% Growth	9.8%	4.0%	14.0%
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(in percentages)			
<b>Unit Case Volume Mix by Category</b>			
Total Carbonated Soft Drinks	96.6%	97.3%	98.6%
Water	1.2	1.4	0.8
Other Categories	2.2	1.3	0.6
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

(in percentages)			
<b>Product Mix by Presentation</b>			
Returnable	24.7%	25.9%	26.9%
Non-returnable and fountain	75.3	74.1	73.1
Jug			
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

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During 2006, Coca-Cola FEMSA's packaging mix continues shifting towards non-returnable presentations. Returnable packaging accounted for 24.7% of total sales volume in Argentina in 2006 as compared to 25.9% in 2005. In 2006, Coca-Cola FEMSA introduced *Dasani*, a no-calorie flavored water to complement its non-carbonated beverage portfolio.

Total sales volume reached 164.9 million unit cases in 2006, an increase of 9.8% compared with 150.1 million in 2005. In 2006, core and premium brands incremental volumes more than offset volume decline of the value protection brands. In Argentina, premium brands consist of diet carbonated soft drinks and *Schweppes*. The majority of the volume growth came from Coca-Cola FEMSA's non-returnable presentations, which represented over 65% of the sales volume increase. In 2006, multiple serving presentations for the carbonated soft drinks remained almost flat at 83.7% as compared to 83.4% in 2005.

**Brazil.** Coca-Cola FEMSA's product portfolio in Brazil consists mainly of *Coca-Cola* trademark beverages and certain products sold under proprietary trademarks and the *Kaiser* beer brand, which it sells and distributes on behalf of FEMSA. In 2006, the per capita consumption of carbonated *Coca-Cola* soft drink products in Brazil was 196 eight-ounce servings.

The following table highlights historical total sales volume and sales volume mix in Brazil:

	Year Ended December 31,		
	2006	2005	2004
	(millions of unit cases)		
<b>Product Sales Volume</b>			
Total	268.7	252.5	227.5
% Growth	6.4%	11.0%	4.8%
(in percentages)			
<b>Unit Case Volume Mix by Category</b>			
Total Carbonated Soft Drinks	91.7%	92.3%	93.4%
Water	7.3	6.9	5.8
Other Categories	1.0	0.8	0.8
Total	100.0%	100.0%	100.0%
(in percentages)			
<b>Product Mix by Presentation</b>			
Returnable	10.5%	8.7%	5.3%
Non-returnable and fountain	89.5	91.3	94.7
Jug			
Total	100.0%	100.0%	100.0%

During 2006, consistent with its strategy of strengthening its returnable base, Coca-Cola FEMSA introduced *Fanta* in a 1.0-liter returnable glass bottle, which together with the rest of the returnable portfolio accounted for almost 40% of its incremental carbonated soft drinks volumes during the year.

Total sales volume was 268.7 million unit cases in 2006, an increase of 6.4% compared to 252.5 million in 2005. This increase included 5.7% carbonated soft drink volume growth during the year. Volume increase was a result of volume growth across all our beverage categories, including strong volume growth from the *Coca-Cola* brand in both returnable and non-returnable presentations, and incremental volumes from our water brand *Crystal* due to increased focus on both brands. In 2006, Coca-Cola FEMSA introduced *Minute Maid Mais*, a juice based product to complement our product portfolio.

Coca-Cola FEMSA sells and distributes the *Kaiser* brands of beer in its territories in Brazil. In January 2006, FEMSA Cerveza acquired an indirect controlling stake in Cervejarias Kaiser Brasil S.A. or Cervejarias Kaiser. Coca-Cola FEMSA has subsequently agreed to continue to



distribute the *Kaiser* beer portfolio and to assume the sales function in São Paulo, Brazil, consistent with the arrangements in place prior to 2004.

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### **Seasonality**

Sales of Coca-Cola FEMSA's products are seasonal, as its sales levels generally increase during the summer months of each country and during the Christmas holiday season. In Mexico, Central America, Colombia and Venezuela, Coca-Cola FEMSA typically achieves its highest sales during the summer months of April through September as well as during the Christmas holidays in December. In Argentina and Brazil, its highest sales levels occur during the summer months of October through March and the Christmas holidays in December.

### **Marketing**

Coca-Cola FEMSA, in conjunction with The Coca-Cola Company, has developed a sophisticated marketing strategy to promote the sale and consumption of its products. It relies extensively on advertising, sales promotions and non-price related retailer incentive programs designed by local affiliates of The Coca-Cola Company to target the particular preferences of its soft drink consumers. Coca-Cola FEMSA's marketing expenses in 2006, net of contributions by The Coca-Cola Company, were Ps. 2,140 million. The Coca-Cola Company contributed an additional Ps. 1,164 million in 2006. Through the use of advanced information technology, Coca-Cola FEMSA has collected customer and consumer information that allows it to tailor its marketing strategies to the types of customers located in each of its territories and to meet the specific needs of the various market segments it serves.

**Retailer Incentive Programs.** Incentive programs include providing retailers with commercial coolers for the display and cooling of soft drink products and for point-of-sale display materials. Coca-Cola FEMSA seeks, in particular, to increase the number of distribution coolers among retailers to increase the visibility and consumption of its products and to ensure that they are sold at the proper temperature. Sales promotions include sponsorship of community activities, sporting, cultural and social events, and consumer sales promotions such as contests, sweepstakes and product giveaways.

**Advertising.** Coca-Cola FEMSA advertises in all major communications media. It focuses its advertising efforts on increasing brand recognition by consumers and improving its customer relations. National advertising campaigns are designed and proposed by The Coca-Cola Company's local affiliates, with Coca-Cola FEMSA's input at the local or regional level.

**Channel Marketing.** In order to provide more dynamic and specialized marketing of its products, Coca-Cola FEMSA's strategy is to segment its market and develop targeted efforts for each segment or distribution channel. Its principal channels are small retailers, on-premise consumption such as restaurants and bars, supermarkets and third party distributors. Presence in these channels entails a comprehensive and detailed analysis of the purchasing patterns and preferences of various groups of soft drink consumers in each of the different types of locations or distribution channels. In response to this analysis, Coca-Cola FEMSA tailors its product, price, packaging and distribution strategies to meet the particular needs of and exploit the potential of each channel.

Coca-Cola FEMSA believes that the implementation of its channel marketing strategy also enables it to respond to competitive initiatives with channel-specific responses as opposed to market-wide responses. This focused response capability isolates the effects of competitive pressure in a specific channel, thereby avoiding costlier market-wide responses. Coca-Cola FEMSA's channel marketing activities are facilitated by its management information systems. It has invested significantly in creating these systems, including in hand-held computers to support the gathering of product, consumer and delivery information, for most of its sales routes in Mexico and Argentina and selectively in other territories.

**Multi-segmentation.** Coca-Cola FEMSA has been implementing a multi-segmentation strategy in the majority of its markets. This strategy consists on the implementation of different product/price/package portfolios by market cluster or group. These clusters are defined based on competitive intensity and socio-economic levels, rather than solely on the types of distribution channels. Coca-Cola FEMSA has developed a market intelligence

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system that it refers to as the right-execution-daily system (RED), which has allowed it to implement this strategy. This system provides the data required to target specific consumer segments and channels and allows it to collect and analyze the data required to tailor its product, package, price and distribution strategies to fit different consumer needs.

**Product Distribution**

The following table provides an overview of Coca-Cola FEMSA's product distribution centers and the retailers to which it sells its products:

**Product Distribution Summary**

as of December 31, 2006

	Mexico	Central America	Colombia	Venezuela	Argentina	Brazil
Distribution Centers	92	28	37	32	5	12
Retailers (in thousands) <sup>(1)</sup>	624.1	115.7	381.1	224.2	79.1	122.3

(1) Estimated.

Coca-Cola FEMSA uses two main sales methods depending on market and geographic conditions: (1) the traditional or conventional truck route system, in which the person in charge of the delivery makes immediate sales from inventory available on the truck and (2) the pre-sale system, which separates the sales and delivery functions and allows sales personnel to sell products prior to delivery and trucks to be loaded with the mix of products that retailers have previously ordered, thereby increasing distribution efficiency. As part of the pre-sale system, sales personnel also provide merchandising services during retailer visits, which Coca-Cola FEMSA believes enhance the presentation of its products at the point of sale. In certain areas, it also makes sales through third party wholesalers of its products. The vast majority of Coca-Cola FEMSA's sales are on a cash basis.

Coca-Cola FEMSA continually evaluates its distribution model in order to fit with the local dynamics of the market place. It is currently analyzing the way we go to market, recognizing different service needs from its customers, while looking for a more efficient distribution model. As part of this strategy, it is rolling out a variety of new distribution models throughout its territories looking for improvements in its distribution network.

Coca-Cola FEMSA believes that service visits to retailers and frequency of deliveries are essential elements in an effective selling and distribution system for its products. Accordingly, Coca-Cola FEMSA has continued to expand its pre-sale system throughout its operations in a selective way.

Coca-Cola FEMSA's distribution centers range from large warehousing facilities and re-loading centers to small deposit centers. In addition to its fleet of trucks, it distributes its products in certain locations through a fleet of electric carts and hand-trucks in order to comply with local environmental and traffic regulations. Coca-Cola FEMSA generally retains third parties to transport its finished products from the bottler plants to the distribution centers.

**Mexico.** Coca-Cola FEMSA contracts with one of our subsidiaries for the transportation of finished products to its distribution centers from its Mexican production facilities. From the distribution centers, Coca-Cola FEMSA then distributes its finished products to retailers through its own fleet of trucks. During 2006, Coca-Cola FEMSA closed 14 out of 106 distribution centers in its Mexican operations.

In Mexico, Coca-Cola FEMSA sells a majority of its beverages at small retail stores to customers who take the beverages home or elsewhere for consumption. It also sells products through the on-premise segment, supermarkets and others. The on-premise segment consists of sales through sidewalk stands, restaurants, bars and various types of dispensing machines as well as sales through point-of-sale programs in concert halls, auditoriums and theaters.

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**Central America.** Coca-Cola FEMSA distributes its finished products to retailers through a combination of its own fleet of trucks and third party distributors. At the end of 2006, it operated 28 distribution centers in its Central American territories. As in most of its territories, in Central American operations, an important part of Coca-Cola FEMSA's total sales volume is through small retailers, and it has low supermarket penetration.

**Colombia.** Coca-Cola FEMSA distributes its finished products to retailers through a combination of its own fleet of trucks and third party distributors. During 2006, Coca-Cola FEMSA closed five distribution facilities in Colombia. This territory also has low supermarket penetration, which means an important part of our total sales volume is through small retailers.

**Venezuela.** Coca-Cola FEMSA distributes its finished products to retailers through a combination of its own fleet of trucks and third party distributors. Its Venezuelan operations distribute a significant part of total sales through small retailers and supermarkets, which in most of its operations have a less significant presence.

**Argentina.** As of December 31, 2006, Coca-Cola FEMSA operated 5 distribution centers in Argentina. It distributes its finished products to retailers through a combination of its own fleet of trucks and third party distributors.

In 2006, Coca-Cola FEMSA sold the majority of its products in the take-home segment, which consists of sales to consumers who take the beverages home or elsewhere for consumption. The percentage of total sales volume through supermarkets remained stable at 14.6% in 2006 from 14.3% in 2005.

**Brazil.** In Brazil, the delivery of Coca-Cola FEMSA's finished products to customers is by a third party. At the end of 2006, it operated 12 distribution facilities in its Brazilian territories. In contrast with the rest of its territories, which have low supermarket penetration, in Brazil Coca-Cola FEMSA sold more than 20% of its total sales volume through supermarkets in 2006. In addition, in designated zones, third-party distributors purchase its products at a discount from the wholesale price and resell the products to retailers.

## **Competition**

Although Coca-Cola FEMSA believes that its products enjoy wider recognition and greater consumer loyalty than those of its principal competitors, the soft drink segments in the territories in which it operates are highly competitive. Its principal competitors are local bottlers of Pepsi and other bottlers and distributors of national and regional soft drink brands. It faces increased competition in many of its territories from producers of low price beverages, commonly referred to as B brands. A number of its competitors in Central America, Argentina and Brazil offer both soft drinks and beer, which may enable them to achieve distribution efficiencies.

Recently, price discounting and packaging have joined consumer sales promotions, customer service and non-price retailer incentives as the primary means of competition among soft drink bottlers. Coca-Cola FEMSA competes by seeking to offer products at an attractive price in the different segments in its markets and by building on the value of its brands. Coca-Cola FEMSA believes that the introduction of new products and new presentations has been a significant competitive technique that allows it to increase demand for its products, provide different options to consumers and increase new consumption opportunities.

**Mexico.** Coca-Cola FEMSA's principal competitors in Mexico are bottlers of Pepsi products, whose territories overlap but are not co-extensive with its own. In central Mexico it competes with a subsidiary of PBG, the largest bottler of Pepsi products globally, and Grupo Embotelladores Unidos, S.A.B. de C.V., the Pepsi bottler in central and southeast Mexico. In addition, Coca-Cola FEMSA competes with Cadbury Schweppes and with other national and regional brands in its Mexican territories. It continues to face competition from low price producers offering multiple serving size presentations in the soft drink industry.

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**Central America.** In the countries that comprise its Central America segment, Coca-Cola FEMSA's main competitors are Pepsi bottlers. In Guatemala and Nicaragua, it competes against a joint venture between AmBev and The Central American Bottler Corporation. In Costa Rica, its principal competitor is Embotelladora Centroamericana, S.A., and in Panama, its main competitor is Refrescos Nacionales, S.A. During 2006, Coca-Cola FEMSA continued to face competition from low price producers offering multiple serving size presentations in some Central American countries.

**Colombia.** Coca-Cola FEMSA's principal competitor in Colombia is Postobón S.A., which we refer to as Postobón, a well-established local bottler that sells flavored soft drinks, some of which have a wide consumption preference, such as cream soda, which is the second most popular category in the Colombian soft drink industry in terms of total sales volume, and that also sells Pepsi products. Postobón is a vertically integrated producer, the owners of which hold other significant commercial interests in Colombia. During 2007, Coca-Cola FEMSA expects to face an increase in competition from low price producers offering multiple serving size presentations.

**Venezuela.** In Venezuela, Coca-Cola FEMSA's main competitor is Pepsi-Cola Venezuela, C.A., a joint venture formed between PepsiCo. and Empresas Polar, S.A., the leading beer distributor in the country. It also competes with the producers of *Kola Real* in part of the country.

**Argentina.** In Argentina, Coca-Cola FEMSA's main competitor is BAESA, a Pepsi bottler, which is owned by Argentina's principal brewery, Quilmes Industrial S.A., and indirectly controlled by AmBev. In addition, it competes with a number of competitors offering generic, low priced soft drinks as well as many other generic products and private label proprietary supermarket brands.

**Brazil.** In Brazil, Coca-Cola FEMSA competes against AmBev, a Brazilian company with a portfolio of brands that includes Pepsi, local brands with flavors such as guaraná and proprietary beers. It also competes against B brands or Tubainas, which are small, local producers of low cost flavored soft drinks in multiple serving presentations that represent an important portion of the soft drink market.

## **Taxation of Soft Drinks**

All of the countries in which Coca-Cola FEMSA operates, except for Panama, impose a value-added tax on the sale of soft drinks, with a rate of 15% in Mexico, 12% in Guatemala, 15% in Nicaragua, 13% in Costa Rica, 16% in Colombia, 14% in Venezuela, 18% (São Paulo) and 17% (Mato Grosso do Sul) in Brazil and 21% in Argentina. In addition, several of the countries in which Coca-Cola FEMSA operates impose the following excise or other taxes:

Guatemala imposes an excise tax of 0.18 cents in local currency (Ps. 0.26 as of December 31, 2006) per liter of soft drink.

Costa Rica imposes a specific tax on non-alcoholic bottled beverages based on the combination of packaging and flavor, a 5% excise tax on local brands, a 10% tax on foreign brands and a 14% tax on mixers.

Nicaragua imposes a 9% tax on consumption.

Panama imposes a 5% tax based on the cost of goods produced.

Argentina imposes an excise tax on colas and on flavored soft drinks containing less than 5% lemon juice or less than 10% fruit juice of 8.7%, and an excise tax on flavored soft drinks with 10% or more fruit juice and on mineral water of 4.2%.

Brazil imposes an average production tax of 16.5% and an average sales tax of 4.6% in the territories where Coca-Cola FEMSA operates.

## **Price Controls**

## Edgar Filing: MEXICAN ECONOMIC DEVELOPMENT INC - Form 20-F

At present, there are no price controls on Coca-Cola FEMSA's products in any of its segments. In Mexico, prior to 1992, prices of carbonated soft drinks were regulated by the Mexican government. From 1992 to 1995,

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the industry was subject to voluntary price restraints. In response to the devaluation of the Mexican peso relative to the U.S. dollar in 1994 and 1995, however, the Mexican government adopted an economic recovery plan to control inflationary pressures in 1995. As part of this plan, the Mexican government encouraged the *Asociación Nacional de Productores de Refrescos y Aguas Carbonatadas, A.C.* (the National Association of Bottlers) to engage in voluntary consultations with the Mexican government with respect to price increases for returnable presentations. These voluntary consultations were terminated in 1996. Formal price controls have been imposed historically in several of the countries in which Coca-Cola FEMSA operates, including in Colombia, Brazil and Venezuela, and could be imposed in the future. The imposition of price controls in the future may limit Coca-Cola FEMSA's ability to set prices and adversely affect its results of operations.

### **Raw Materials**

Pursuant to the bottler agreements with The Coca-Cola Company, Coca-Cola FEMSA is required to purchase concentrate, including aspartame, an artificial sweetener used in diet sodas, for all *Coca-Cola* trademark beverages from companies designated by The Coca-Cola Company. The price of concentrate for all *Coca-Cola* trademark beverages is a percentage of the average price Coca-Cola FEMSA charges to its retailers in local currency net of applicable taxes. Although The Coca-Cola Company has the right to unilaterally set the price of concentrates, in practice this percentage has historically been set pursuant to periodic negotiations with The Coca-Cola Company. In most cases, concentrate is purchased in the local currency of the territory.

In 2005, The Coca-Cola Company decided to gradually increase concentrate prices for carbonated soft drinks over a three year period in Mexico beginning in 2007, and in Brazil in 2006. As part of the new cooperation framework that Coca-Cola FEMSA arrived at with The Coca-Cola Company at the end of 2006, The Coca-Cola Company will provide a relevant portion of the funds derived from the incidence increase to marketing support of the carbonated and non-carbonated soft drinks portfolio.

In addition to concentrate, Coca-Cola FEMSA purchases sweeteners, carbon dioxide, resin and ingots to make plastic bottles, finished plastic and glass bottles, cans, closures and fountain containers, as well as other packaging materials. Sweeteners are combined with water to produce basic syrup, which is added to the concentrate as the sweetener for the soft drink. Coca-Cola FEMSA's bottler agreements provide that, with respect to *Coca-Cola* trademark beverages, these materials may be purchased only from suppliers approved by The Coca-Cola Company. Prices for packaging materials and high fructose corn syrup historically are determined with reference to the U.S. dollar, although the local currency equivalent in a particular country is subject to price volatility in accordance with changes in exchange rates. Coca-Cola FEMSA's most significant packaging raw material costs arise from the purchase of resin, plastic ingots to make plastic bottles and finished plastic bottles, which it obtains from international and local producers. The prices of these materials are tied to crude oil prices and global resin supply, and in previous years it has experienced volatility in the prices it pays for these materials. In Mexico, its average price for resin started to decline in the second half of 2006, and Coca-Cola FEMSA currently expects prices to remain stable for 2007.

Under Coca-Cola FEMSA's agreements with The Coca-Cola Company, it may use raw or refined sugar or high fructose corn syrup as sweeteners in its products. Sugar prices in all of the countries in which it operates, other than Brazil, are subject to local regulations and other barriers to market entry that cause it to pay in excess of international market prices for sugar in certain countries. Coca-Cola FEMSA has experienced sugar price volatility in these territories as a result of changes in local conditions, regulations and the stronger correlation to oil prices recently due to the use of sugar in alternative fuels.

None of the materials or supplies that Coca-Cola FEMSA uses is presently in short supply, although the supply of specific materials could be adversely affected by strikes, weather conditions, governmental controls or national emergency situations.

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**Mexico.** Coca-Cola FEMSA purchases its returnable plastic bottles from Continental PET Technologies de México, S.A. de C.V., a subsidiary of Continental Can, Inc., which has been the exclusive supplier of returnable plastic bottles to The Coca-Cola Company and its bottlers in Mexico. Coca-Cola FEMSA also primarily purchases resin from Arteva Specialties, S. de R.L. de C.V. and Industrias Voridian, S.A. de C.V., which ALPLA Fábrica de Plásticos, S.A. de C.V., known as ALPLA, manufactures into non-returnable plastic bottles for it.

Coca-Cola FEMSA primarily purchases sugar from Promotora Mexicana de Embotelladoras, S.A. de C.V., known as PROMESA, a cooperative of *Coca-Cola* bottlers. These purchases are regularly made under one-year agreements between PROMESA and each bottler subsidiary for the sale of sugar at a price that is determined monthly based on the cost of sugar to PROMESA. Coca-Cola FEMSA also purchases sugar from Beta San Miguel, S.A. de C.V., a sugar cane producer in which it holds a 2.54% equity interest.

In December 2001, the Mexican government expropriated the majority of the sugar mills in Mexico. To manage this industry, the Mexican government entered into a trust agreement with Nacional Financiera, S.N.C., which it refers to as Nafin, a Mexican government-owned development bank, pursuant to which Nafin acts as trustee. In addition, the Mexican government imposed a 20% excise tax, effective January 1, 2002, on carbonated soft drinks sweetened with high fructose corn syrup. As a result, Coca-Cola FEMSA converted its Mexican bottler facilities to sugar cane-based production in early 2002. On January 1, 2003, the Mexican government broadened the reach of this tax by imposing a 20% excise tax on carbonated soft drinks produced with non-sugar sweetener. The effect of these excise taxes was to limit Coca-Cola FEMSA's ability to substitute other sweeteners for sugar. Coca-Cola FEMSA initiated proceedings in Mexican federal court against this excise tax that allowed it to cease paying the tax in 2005 and 2006. It also resumed the use of high fructose corn syrup as a sweetener. At the end of 2006, effective beginning in 2007, the Mexican government removed this excise tax and the government recently agreed to return the expropriated mills to their former owners. This process has begun and the majority of mills have been returned to these owners.

Imported sugar is also presently subject to import duties, the amount of which is set by the Mexican government. As a result, sugar prices in Mexico are in excess of international market prices for sugar. In 2005, sugar prices remained stable after significant increases in 2004, however, in 2006 prices increased again. Coca-Cola FEMSA expects volatility in sugar prices in Mexico in 2007 due to local regulations and other market barriers to entry.

**Central America.** The majority of Coca-Cola FEMSA's raw materials such as glass and plastic bottles and cans are purchased from several local suppliers. Sugar is available from one supplier in each country. Local sugar prices in certain Central American countries are significantly higher than international market prices and Coca-Cola FEMSA's ability to import sugar or high fructose corn syrup is limited.

**Colombia.** Coca-Cola FEMSA uses sugar as a sweetener in its products, which it buys from several domestic sources. It purchases pre-formed ingots from Amcor and Tapón Corona de Colombia S.A. It purchases all its glass bottles and cans from suppliers, in which its competitor Postobón owns a 40% equity interest. While other suppliers exist for glass bottles, cans are available only from this one source.

**Venezuela.** Coca-Cola FEMSA uses sugar as a sweetener in its products, which it purchases primarily from the local market. Since 2003, it has experienced a sugar shortage due to lower domestic production and the inability of the predominant sugar importers to obtain permissions to import. However, it was able to meet its sugar requirements through imports. Coca-Cola FEMSA buys glass bottles from one supplier, Productos de Vidrio, S.A., a local supplier, but there are other alternative suppliers authorized by The Coca-Cola Company. Coca-Cola FEMSA has several supplier options for plastic non-returnable bottles but it acquires most of its requirements from ALPLA de Venezuela, S.A.

**Argentina.** In Argentina, Coca-Cola FEMSA uses high fructose corn syrup from several different local suppliers as a sweetener in its products instead of sugar. It purchases glass bottles, plastic cases and other raw



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materials from several domestic sources. It purchases pre-formed plastic ingots, as well as returnable plastic bottles, at competitive prices from Embotelladora del Atlántico S.A., a local subsidiary of Embotelladora Andina S.A., a *Coca-Cola* bottler with operations in Argentina, Chile and Brazil, and other international suppliers. Coca-Cola FEMSA purchases its can presentations and juice-based products for distribution to customers in Buenos Aires from CICAN S.A., in which it owns a 48.1% equity interest.

**Brazil.** Sugar is widely available in Brazil at local market prices, which historically have been lower than international prices. Coca-Cola FEMSA experienced significant increases in sugar prices in the first half of the year, due to increases in oil prices. In the second half of the year sugar prices declined almost in the same proportion of the previous increase. It expects sugar prices to remain stable in Brazil during 2007. Coca-Cola FEMSA purchases glass bottles, plastic bottles and cans from several domestic and international suppliers.

## **FEMSA Cerveza**

### **Overview and Background**

FEMSA Cerveza produces beer in Mexico and Brazil and exports its products to more than 50 countries worldwide, with North America being its most important export market, followed by certain markets in Europe, Latin America and Asia. In 2006, FEMSA Cerveza was ranked the thirteenth-largest brewer in the world in terms of sales volume. In Mexico, its main market, FEMSA Cerveza is the second largest beer producer in terms of sales volume. In 2006, approximately 69% of FEMSA Cerveza's sales volume came from Mexico, with the remaining 24% from Brazil and 7% from exports. In 2006, FEMSA Cerveza sold 37.697 million hectoliters of beer.

FEMSA Cerveza's principal operating subsidiaries are Cervecería Cuauhtémoc Moctezuma, S.A. de C.V., which operates six breweries in Mexico, Cervejarias Kaiser Brasil S.A., or Kaiser, which operates eight breweries in Brazil, and Cervezas Cuauhtémoc Moctezuma, S.A. de C.V., which operates our company-owned distribution centers across Mexico.

Our management believes that Brazil is one of the most attractive and profitable beer markets in the world. Accordingly, in January 2006, FEMSA Cerveza acquired a 68% equity stake in the Brazilian brewer Kaiser from The Molson Coors Brewing Co., or Molson Coors, for US\$68 million, at the same time receiving indemnity rights for certain tax contingencies of Kaiser. Molson Coors later completed its exit from the Brazilian market in December 2006 by exercising a put option to sell its 15% stake in Kaiser to FEMSA Cerveza for US\$15.6 million. Under the terms of the agreements governing FEMSA Cerveza's original acquisition of Kaiser in January 2006, FEMSA Cerveza's indemnity rights for certain tax contingencies provided by Molson Coors increased proportionately with the incremental 15% stake it acquired. In addition, on December 22, 2006, FEMSA Cerveza completed a capital increase of US\$200 million in Kaiser, following the successful settlement of tax contingencies with Brazilian state and federal tax authorities. The capital increase completed the capitalization of Kaiser, which we believe will significantly strengthen Kaiser's balance sheet and allow us to continue to expand our operations in Brazil. FEMSA Cerveza was the only shareholder to participate in the capital increase, and as a result of these transactions, FEMSA Cerveza owns as of May 31, 2007, 99.83% of the equity of Kaiser. Heineken N.V. elected not to participate in the increase, thereby diluting its 17% interest in Kaiser to 0.17%.

### **Beer Sales Volume**

FEMSA Cerveza volume figures contained in this annual report refer to invoiced sales volume of beer. In Mexico, invoiced sales volume represents the quantity of hectoliters of beer sold by FEMSA Cerveza's breweries to unaffiliated distributors and by affiliated distributors to retailers. In Brazil, invoiced sales volume represents the quantity of hectoliters of beer sold by Kaiser. Kaiser sells its products to the Brazilian *Coca-Cola* bottlers, which sell and distribute Kaiser beers in their respective territories. The term hectoliter means 100 liters or approximately 26.4 U.S. gallons.

FEMSA Cerveza's total beer sales volume totaled 37.697 million hectoliters in 2006, an increase of 39.5% from total sales volume of 27.018 million hectoliters in 2005. In 2006, FEMSA Cerveza's Mexican beer

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sales volume increased by 5.6% to 25.951 million hectoliters and export beer sales volume increased by 15.3% to 2,811 million hectoliters. Brazil sales volume prior to 2006 is not reported as the operation was not owned or operated by FEMSA Cerveza before January 2006.

**FEMSA Cerveza Total Beer Sales Volumes**

	Year Ended December 31,				
	2006	2005	2004	2003	2002
	(in thousands of hectoliters)				
Mexico beer sales volume	25,951	24,580	23,442	22,582	21,856
Brazil beer sales volume	8,935	NA	NA	NA	NA
Export beer sales volume	2,811	2,438	2,240	1,982	1,955
Total beer sales volume	37,697	27,018	25,682	24,564	23,811

FEMSA Cerveza's Mexican beer sales volume recorded a compounded average growth rate of 4.4% for the period of 2002 through 2006. This compares with the 3.3% compounded average growth rate of the Mexican gross domestic product for the same period. Mexican beer sales for the same period recorded a 4.2% compounded average growth rate. FEMSA Cerveza's export sales volume recorded a compound average growth rate of 9.5% for the same period, while the compound average growth rate for export sales was 17.6%.

**Femsa Cerveza's Strategy**

In order to achieve its objectives in the Mexican market, FEMSA Cerveza seeks to:

*implement advanced brand, packaging and price information gathering techniques* at the point-of-sale to allow FEMSA Cerveza to fine tune its portfolio of brands and pricing at the level of individual retailers;

*innovate through a differentiated brand portfolio and increase the value of its brands* by tailoring its portfolio of brands based on the attributes of each brand to specific markets using marketing techniques such as market segmentation, brand positioning and distinctive advertising campaigns;

*establish profitable, long-term relationships with retailers* by implementing client-specific strategies to help increase their sales and profitability, such as modifying commercial terms with retailers, promotions and types of refrigeration equipment and point-of-sale marketing materials;

*achieve balanced and profitable retail distribution levels* by selecting the appropriate mix of on- and off-premise accounts, and a balance of image-focused accounts (like upscale restaurants) and volume-driven accounts (like beer depots); and

*pursue additional efficiencies and cost reductions on a continuing basis* from production to final distribution, by pursuing specific cost reduction efforts, using information technology and improving business processes.

**Mexico Operations****The Mexican Beer Market**

The Mexican beer market was the eighth largest beer market in the world in terms of industry sales volume in 2006 and is characterized by (1) concentrated domestic beer production, (2) regional market share differences, (3) the prevalence of government licensing regulations and (4) favorable demographics in the beer drinking population.



**Table of Contents*****Concentrated Mexican beer production***

Since 1985, Mexico has effectively had only two independent domestic beer producers, FEMSA Cerveza and Grupo Modelo. Grupo Modelo, a publicly traded company based in Mexico City, is the holding company of 76.8% of Diblo, S.A. de C.V., which operates the brewing and packaging subsidiaries of Grupo Modelo. Grupo Modelo's principal beer brands are *Corona*, *Modelo*, *Victoria* and *Pacifico*. Grupo Modelo's *Corona*, *Modelo* and *Victoria* brands are distributed nationwide in Mexico, while *Pacifico* is sold principally along the pacific coastal regions. Modelo Especial, Modelo Light and Pacifico are Grupo Modelo's domestic can presentations. FEMSA Cerveza's sales in the Mexican market depend on its ability to compete with Grupo Modelo.

Historically, beer imports have not been a significant factor in the Mexican beer market, because they were subject to tariffs of up to 20%. Under NAFTA, the tariff on imported beer from the United States and Canada was gradually reduced and eventually eliminated in January 2001. Notwithstanding the reduction in tariff levels, imported beers accounted for approximately 2.1% of the total Mexican beer market in terms of sales volume during 2006. FEMSA Cerveza believes that tariff elimination has had a limited effect on the Mexican beer market because imported beers are largely premium and super-premium products sold in aluminum cans, which are a more expensive means of packaging in Mexico than beer sold in returnable bottles. Periods of relative strength of the Mexican peso with respect to the U.S. dollar, however, may lower the price of imported beer to consumers and may result in increased demand for imported beer in the Mexican market.

***Regional market share differences***

FEMSA Cerveza and Grupo Modelo are both strongest in beer markets in separate regions of Mexico. FEMSA Cerveza has a stronger market position in the northern and southern areas of Mexico while Grupo Modelo has a stronger market position in central Mexico. We believe that these regional market positions can be traced in part to consumer loyalty to the brand of beer that has historically been associated with a particular region. For example, FEMSA Cerveza's *Carta Blanca* brand was first produced in Monterrey, Nuevo León in 1891. The strong regional identity in Monterrey and surrounding northeastern areas is reflected in the region's preference for *Carta Blanca* and other FEMSA Cerveza brands.

We also believe that regional market strength is a function of the proximity of the breweries to the markets they serve. Transportation costs restrict the most efficient distribution of beer to a geographic area of approximately 300 to 500 kilometers surrounding a brewery. Generally, FEMSA Cerveza commands a majority of the beer sales in regions that are nearest to its largest breweries. FEMSA Cerveza's largest breweries are in Orizaba, Veracruz and in Monterrey, Nuevo León. Grupo Modelo's largest breweries are located in Mexico City, Oaxaca and Zacatecas.

The northern region of Mexico has traditionally enjoyed a higher per capita income level, attributable in part to its rapid industrialization within the last 50 years and to its commercial proximity to the United States. In addition, FEMSA Cerveza believes that per capita beer consumption is also greater in this region due to its warmer climate and a more ingrained beer culture.

**Mexican Regional Demographic Statistics**

<b>Region</b>	<b>Percent of 2006 Total Population</b>	<b>Percent of Total 2006 Gross Domestic Product</b>	<b>Per Capita 2006 Gross Domestic Product</b>
Northern	26.4%	33.5%	Ps. 101.3
Southern	22.7	15.2	53.3
Central	50.9	51.3	80.1
Total	100.0%	100.0%	Ps. 79.6

Source: FEMSA Cerveza estimates based on figures published by the Mexican Institute of Statistics (INEGI) and CAPEM Oxford Economics Forecasting.

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### ***Government regulation***

The Mexican federal government regulates beer consumption in Mexico primarily through taxation while local governments in Mexico regulate primarily through the issuance of licenses that authorize retailers to sell alcoholic beverages.

Federal taxes on beer consisted of a 25% excise tax and a 15% value-added tax, which together represented 43.75% of the total pre-tax price of beer to retailers. In 2005, the excise tax was amended for the first time since January 1998. Effective January 1, 2006, the excise tax is the higher of (1) 25% and (2) Ps. 3 per liter for non-returnable presentation or Ps. 1.74 for returnable presentations, as part of an environmental initiative by the Mexican governmental to encourage returnable presentations. The tax component of retail beer prices is significantly higher in Mexico than in the United States.

The number of retail outlets authorized to sell beer is controlled by local jurisdictions, which issue licenses authorizing the sale of alcoholic beverages. Other regulations regarding beer consumption in Mexico vary according to local jurisdiction and include limitations on the hours during which restaurants, bars and other retail outlets are allowed to sell beer and other alcoholic beverages. FEMSA Cerveza has been engaged in addressing these limitations at various levels, including efforts with governmental and civil authorities to promote better education for the responsible consumption of beer. For instance, as part of its ongoing community activities, FEMSA Cerveza has been an active sponsor of a nationwide designated driver program in Mexico.

Since July 1984, Mexican federal regulation has required that all forms of beer packaging carry a warning advising that excessive consumption of beer is hazardous to one's health. In addition, the *Ley General de Salud* (the General Health Law), requires that all beers sold in Mexico maintain a sanitation registration with the *Secretaría de Salud* (the Ministry of Health).

### ***Demographics of beer drinking population***

We estimate that annual per capita beer consumption for the total Mexican population reached approximately 58 liters in 2006, as compared to approximately 81 liters in the United States. The legal drinking age is 18 in Mexico. We consider the population segment of men between the ages of 18 and 45 to be FEMSA Cerveza's primary market. At least 38% of the Mexican population is under the age of 18 and, therefore, is not considered to be part of the beer drinking population.

Based on historical trends and what management perceives as the continued social acceptance of beer consumption, FEMSA Cerveza believes that general population growth will result in an increase in the number of beer consumers in Mexico. Based on historical trends as measured by the Mexican Institute of Statistics, we expect the Mexican population to grow at an average annual rate of approximately 1.2% per year over the period from 2007 to 2011. We estimate that over the next 10 years approximately in excess of 1.6 million additional people per year will become potential beer consumers due to the natural aging of the Mexican population.

### ***Macroeconomic influences affecting beer consumption***

We believe that consumption activity in the Mexican beer market is heavily influenced by the general level of economic activity in Mexico, the country's gross wage base, changes in real disposable income and employment levels. As a result, the beer industry reacts sharply to economic change. The industry generally experiences high volume growth in periods of economic strength and slower volume growth or volume contraction in periods of economic weakness. Domestic beer sales declined in Mexico in 1982, 1983 and 1995. These sales decreases correspond to periods in which the Mexican economy experienced severe disruptions. Similarly, the economic slowdown observed in 2002 corresponded to a reduction in domestic beer sales in 2002. In 2003, given the effect of a continued economic slowdown on consumers, FEMSA Cerveza decided not to increase prices. The reduction in prices in real terms (after giving effect to inflation) was the main driver for increasing sales volumes during 2003. In 2004, growth in Mexico's gross domestic product was the main driver for increasing beer sales volume, despite price increases in nominal terms in the Mexican beer industry. In 2005 and 2006, beer sales volume growth outpaced growth in Mexico's gross domestic product. In 2006, beer sales volume growth was the highest in the last ten years due to the strong economy, which boosted consumption of our products.

**Table of Contents****Beer Prices**

After more than 18 months without a price increase, FEMSA Cerveza increased prices in Mexico during the first quarter of 2004. The effect of these price increases was partially offset by promotional activity that reduced the price of beer, due to a strong competitive environment. During 2005, FEMSA Cerveza increased prices in Mexico in line with inflation. In the first quarter of 2006, FEMSA Cerveza increased prices in Mexico by region, brand, presentation and point of sale, resulting in an average price increase of 3.5% in nominal Mexican peso terms. During 2007, FEMSA Cerveza continues with its segmentation strategy and revenue management and will continue exploring opportunities to improve price, considering the specific conditions of each market.

According to the Bank of Mexico's consumer beer price index, for the Mexican beer industry as a whole, average consumer beer prices increased 3.5% in nominal terms, which represents no price increase in real terms. The following table shows relative real average retail prices since 2002 for the Mexican beer industry:

**Mexican Beer Industry****Cumulative Real Consumer Beer Price Index: 2002-2006**

(2002 = 100%)

Year Ended December 31,					
2006	2005	2004	2003	2002	
91.3	91.4	94.4	96.3	100.0	

Source: Bank of México

**Product Overview**

As of December 31, 2006, in Mexico FEMSA Cerveza produced and/or distributed 18 brands of beer in 13 different presentations resulting in a portfolio of 88 different product offerings. The most important brands in FEMSA Cerveza's Mexican portfolio include: *Tecate*, *Sol*, *Carta Blanca*, *Superior* and *Indio*. These five brands, all of which are distributed nationwide in Mexico, accounted for approximately 94% of FEMSA Cerveza's Mexico beer sales volume in 2006.

Per capita information, product segments, relative prices and packaging information with respect to FEMSA Cerveza have been computed and are based upon our statistics and assumptions.

**Beer Presentations**

In its Mexican operations, FEMSA Cerveza produces and distributes beer in returnable glass bottles and kegs and in non-returnable aluminum cans and glass bottles. FEMSA Cerveza uses the term presentation to reflect these packaging options. The following table shows the percent of beer sales volume by presentation for the year ended December 31, 2006:

**FEMSA Cerveza's Beer Volume by Presentation, Mexican breweries****Year Ended December 31, 2006**

Presentation	Percentage
Returnable bottles	57.7%
Non-returnable presentations	40.5
Kegs	1.8
Total	100.0%



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### ***Returnable presentations***

The most popular form of packaging in the Mexican beer market is the returnable bottle. FEMSA Cerveza believes that the popularity of the returnable bottle is attributable to its lower price to the consumer. While returnable bottles generally cost approximately twice as much to produce as non-returnable bottles, returnable bottles may be reused an average of 30 times before being recycled. As a result, beer producers are able to charge lower prices for beer in returnable bottles. Because non-returnable presentations are the most expensive, we believe that demand for these presentations is highly sensitive to economic factors. During periods when the Mexican economy is weak, returnable sales volume generally increase at a faster rate relative to non-returnable sales volume.

### ***Non-returnable presentations***

FEMSA Cerveza's presentation mix in Mexico has been growing in non-returnable presentations in the last few years, as we tailor our offering to consumer preferences and provide different convenient alternatives. The vast majority of export sales are in non-returnable presentations.

### **Relative Pricing**

Returnable bottles and kegs are the least expensive beer presentation on a per-milliliter basis. Cans and non-returnable bottles have historically been priced higher than returnable bottles. In 2006, the weighted average of this difference was between 25% and 30% higher price per-milliliter for non-returnable presentations. The consumer preference for presentations in cans has varied considerably over the past 20 years, rising in periods of economic prosperity and declining in periods of economic austerity, reflecting the price differential between these forms of packaging.

### **Seasonality**

Demand for FEMSA Cerveza's beer is highest in the Mexican summer season, and consequently, brewery utilization rates are at their highest during this period. Demand for FEMSA Cerveza's products also tends to increase in the month of December, reflecting consumption during the holiday season. Demand for FEMSA Cerveza's products decreases during the months of November, January and February primarily as a result of colder weather in the northern regions of Mexico.

### **Primary Distribution**

FEMSA Cerveza's primary distribution in Mexico is from its production facilities to its distribution centers' warehouses. FEMSA Cerveza delivers to a combination of company-owned and third party distributors. In an effort to improve the efficiency and alignment of the distribution network, FEMSA Cerveza has adjusted its relationship with independent distributors by implementing franchise agreements and as a result, has achieved economies of scale through integration with FEMSA Cerveza's operating systems. FEMSA Cerveza has also increased the number of company-owned distribution centers by acquiring third party distributors in recent years. Through a series of transactions completed in 2006, FEMSA Cerveza increased its directly distributed volume in respect of its Mexican beer sales volume to 82%, operating through 251 company-owned distribution centers. The remaining 19% of the beer sales volume was sold through 68 independent distributors, most of them operating under franchise agreements with FEMSA Cerveza. A franchise agreement is offered only to those distributors that meet certain standards of operating capabilities, performance and alignment. FEMSA Cerveza has historically and intends to continue in the future to acquire those distributors that do not meet these standards. Through this initiative FEMSA Cerveza will continue to seek to increase its Mexico beer sales volume through company-owned distribution centers.

In addition to distributing its own brands, on June 22, 2004, FEMSA Cerveza's brewing subsidiary and Coors Brewing Company entered into an agreement pursuant to which FEMSA Cerveza's subsidiary was appointed the exclusive importer, distributor, marketer and seller of *Coors Light* beer in Mexico.



**Table of Contents****Retail Distribution**

The main sales outlets for beer in Mexico are small, independently-owned mom and pop grocery stores, dedicated beer stores or depósitos, liquor stores and bars. Supermarkets account for only a small percentage of beer sales in Mexico. In addition, FEMSA Comercio operates a chain of more than 4,847 convenience stores under the trade name Oxxo that exclusively sell FEMSA Cerveza's brands.

**Distribution of FEMSA Cerveza Mexico Beer Sales Volume by Outlet****Year Ended December 31, 2006**

<b>Points of Sale</b>	<b>Percentage</b>
Small grocery stores	22%
Beer and liquor stores	26
Mini-markets and convenience stores	21
Other points of sale	9
<b>Subtotal</b>	<b>78%</b>
<b>Consumption Centers</b>	<b>Percentage</b>
Bars	10%
Restaurants	4
Nightclubs	2
Other consumption centers	6
<b>Subtotal</b>	<b>22%</b>
<b>Total</b>	<b>100.0%</b>

The Mexican retail market is fragmented and characterized by a preponderance of small outlets that are unable and unwilling to maintain meaningful inventory levels. Consequently, FEMSA Cerveza must make frequent product deliveries to its retailers. In recent years, FEMSA Cerveza has implemented the pre-sale process of distribution in its markets to improve its distribution practices. The pre-sale process is a distribution method in which the sales and delivery functions are separated and trucks are loaded with the actual mix of products that retailers have previously ordered. One of the primary objectives of pre-sale is to separate sales from distribution to ensure more reliable market access and to enhance efficiency by reducing the number of secondary distribution routes in otherwise highly fragmented markets. Where pre-sale has been implemented, we have experienced a significant reduction in unsold product and a net reduction in distribution personnel. The existence of the pre-sale process facilitates systematic product delivery and helps discipline product inventory at the point-of-sale. Furthermore, pre-sale has enabled FEMSA Cerveza to collect customer and consumer information directly from the marketplace, which then becomes valuable in defining brand portfolios by channel. See Marketing Strategy.

During 2004, FEMSA Cerveza completed the implementation of the pre-sale process in its company-owned distribution centers. As of December 31, 2006, 86% of the beer sales volume of FEMSA Cerveza was sold through the pre-sale process. As of December 31, 2006, FEMSA Cerveza serves more than 320,000 retailers in Mexico and its distribution network operates approximately 2,044 retail distribution routes.

**Enterprise Resource Planning**

FEMSA Cerveza operates an Enterprise Resource Planning system, or ERP, that provides an information and control platform to support commercial activities nationwide in Mexico and correlate them with the administrative and business development decision-making process occurring in FEMSA Cerveza's central office. The Mexican beer sales volume of all FEMSA Cerveza's company-owned distribution centers is operating through ERP, except for third-party distributors acquired during 2006 that will be operating through ERP as of October 2007.



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### **Marketing Strategy**

FEMSA Cerveza focuses on the consumer by segmenting its markets and positioning its brands, accordingly, striving to develop brand and presentation portfolios that provide the best alternatives for every consumption occasion at the appropriate price points. By segmenting its markets, we refer to the technique whereby we target a particular group of consumers with specific characteristics such as lifestyle, attitude, geographic region or age group. Continuous market research provides feedback that is used to evolve and adapt our product offerings to best satisfy our consumers' needs. We are increasingly focused on micro-segmentation, where we use our market research and our information technology systems to target smaller market segments, including in some cases the individual point-of-sale.

FEMSA Cerveza also focuses on the retailer by designing and implementing channel marketing at the point-of-sale, such as promotional programs providing merchandising materials, and, where appropriate, refrigeration equipment. A channel refers to a point-of-sale category, or sub-category, such as supermarkets, beer depots, restaurants, etc. Furthermore, we are always attempting to develop new channels in order to capture incremental consumption opportunities for our brands.

In order to coordinate the brand and channel strategies, we are developing and implementing integrated marketing programs, which aim to improve brand value through the simultaneous use of mass media advertising and targeted marketing efforts at the point-of-sale as well as event sponsorships. Our marketing program for a particular brand seeks to emphasize in a consistent manner the distinctive attributes of that brand.

FEMSA Cerveza has developed a process called Innovation to efficiently enable corporate growth strategies. Innovation is a system-wide priority for FEMSA Cerveza and is developed integrally across all areas of the demand chain to maximize value generation at every stage of demand. Innovation is driven by robust consumer and market research practices that help FEMSA Cerveza identify, develop and execute ideas that deliver value.

### **Plants and Facilities**

FEMSA Cerveza currently operates six breweries in Mexico with an aggregate monthly production capacity of 2.8 million hectoliters, equivalent to approximately 33.7 million hectoliters of annual capacity. Each of FEMSA Cerveza's Mexican breweries has received ISO 9002 certification and a Clean Industry Certification (*Industria Limpia*) given by Mexican environmental authorities. A key consideration in the selection of a site for a brewery is its proximity to potential markets, as the cost of transportation is a critical component of the overall cost of beer to the consumer. FEMSA Cerveza's Mexican breweries are strategically located across the country, as shown in the table below, to better serve FEMSA Cerveza's distribution system.

**Table of Contents****FEMSA Cerveza Mexico Facility Capacity Summary****Year Ended December 31, 2006**

	<b>Average Annualized Capacity (in thousands of hectoliters)</b>
<b>Brewery</b>	
Monterrey	7,800
Orizaba	7,200
Toluca	5,400
Navojoa	5,400
Tecate	4,680
Guadalajara	3,216
<b>Total</b>	<b>33,696</b>
 Average capacity utilization	 83.6%

Between 2002 and 2006, FEMSA Cerveza increased its average monthly production capacity by approximately 120,000 hectoliters through additional investments in existing facilities.

During 2005, FEMSA Cerveza opened a new malt production facility in Puebla, Mexico, increasing its malting capacity by 16% to 154,000 tons per year. This facility covers an area of 18,000 square meters and is one of the largest and most technologically advanced in the world.

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FEMSA Cerveza operates seven effluent water treatment systems in Mexico to treat the water used by the breweries, all of which are wholly owned by FEMSA Cerveza except for the effluent treatment system at the Orizaba brewery, which is a joint venture among FEMSA Cerveza, several other local companies and the government of the state of Veracruz.

**Glass Bottles and Cans**

FEMSA Cerveza produces (1) beverage cans and can ends, (2) glass bottles and (3) crown caps for glass bottle presentations principally to meet the packaging needs of its Mexican operations. The packaging operations include a silica sand mine, which provides materials necessary for the production of glass bottles. The following table provides a summary of the facilities for these operations:

**FEMSA Cerveza Mexico Glass Bottle and Beverage Can Operations Product Summary****Year Ended December 31, 2006**

<b>Product</b>	<b>Location</b>	<b>Annual Production Capacity<sup>(1)</sup></b>	<b>% Average Capacity Utilization</b>
Beverage cans	Ensenada	1,700	100.0
	Toluca	1,800	100.0
		3,500	100.0
Can ends	Monterrey	4,300	98.2
Crown cap	Monterrey	18,000	91.0
Glass bottles	Orizaba	1,300	88.3
Bottle decoration	Nogales	330	56.3
Silica sand	Acayucan	360	100.0

(1) Amounts are expressed in millions of units of each product, except for silica sand which is expressed in thousands of tons.

Two plants produce aluminum beverage can bodies at production facilities in Ensenada and Toluca, and another plant produces can ends at a production facility in Monterrey. During 2006, 56.7% of the beverage can volume produced by these plants was used by FEMSA Cerveza and the remaining amount was sold to third parties.

Glass bottles are produced at a glass production facility in Orizaba, Veracruz and bottles are decorated at a plant in Nogales, Veracruz. During 2006, 75.3% of the glass bottle volume produced by these plants was used by FEMSA Cerveza, 16.7% was sold to Coca-Cola FEMSA and the remaining 8.0% was sold to third parties.

**Raw Materials**

Malted barley, hops, certain grains, yeast and water are the principal ingredients used in manufacturing FEMSA Cerveza's beer products. The principal raw materials used by FEMSA Cerveza's packaging operations include aluminum, steel and silica sand. All of these raw materials are generally available in the open market. FEMSA Cerveza satisfies its commodity requirements through purchases from various sources, including purchases pursuant to contractual arrangements and purchases in the open market.

Aluminum and steel are two of the most significant raw materials used in FEMSA Cerveza's packaging operations to make aluminum cans, can ends and bottle caps. FEMSA Cerveza purchases aluminum and steel directly from international and local suppliers on a contractual basis. These contracts generally have terms of six months or one year and specify prices free-on-board at FEMSA Cerveza's facilities. Companies such as Alcoa, Nittetsu-Shoji, Noreli, CSN, Rasselstein and AHMSA have been selected as suppliers. Prices for aluminum have been volatile in recent periods, and market prices increased approximately 35% in 2006. Prices of aluminum and steel are generally quoted in U.S. dollars, and FEMSA Cerveza's cost is therefore affected by changes in exchange rates. For example, a depreciation of the Mexican peso against the U.S. dollar will increase the cost to FEMSA Cerveza of aluminum and steel, and will decrease FEMSA Cerveza's margins as its sales are generally denominated in Mexican pesos. To date, FEMSA Cerveza's silica sand mine has been able to satisfy all of the silica sand requirements of its glass bottle operations.

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Barley is FEMSA Cerveza's most significant raw material for the production of its beer products. International markets determine the prices and supply sources of agricultural raw materials, which are affected by the level of crop production, inventories, weather conditions, domestic and export demand, as well as government regulations affecting agriculture. The principal source of barley for the Mexican beer industry is the domestic harvest. If domestic production in Mexico is insufficient to meet the industry's requirements, barley (or its equivalent in malt) can be obtained from international markets. Before 2003, pursuant to NAFTA, an annual duty-free import quota for barley (or its equivalent in malt) was set. In 2003, under NAFTA, barley imports from the U.S. and Canada are tax-free and there are no import quota restrictions. Prior to NAFTA, Mexican barley prices were significantly higher than international barley prices. Since the implementation of NAFTA, domestic barley prices in Mexico have been stabilizing considering international references, freights and import expenses. We have generally been able to obtain our barley requirements in the Mexican market. Hops is the only ingredient that is not available domestically in Mexico. FEMSA Cerveza imports hops primarily from the United States and Europe.

## **Brazil Operations**

### **The Brazilian Beer Market**

The Brazilian beer market was the fourth largest beer market in the world in terms of industry sales volume in 2006 and is characterized by (1) concentrated domestic beer production, (2) favorable demographics in the beer drinking population, and (3) a fragmented retail channel.

#### ***Concentrated Brazilian beer production***

The Brazilian beer market is comprised of one very large producer, three medium sized producers, and some minor regional brewers. The very large producer is Companhia de Bebidas das Americas or AmBev, a publicly traded company based in Sao Paulo that is majority-owned by the Belgian brewer Inbev. AmBev's principal beer brands are *Skol*, *Brahma* and *Antartica*. AmBev is also a large bottler of carbonated soft drinks, with brands such as *Guaraná Antartica* and *Pepsi Cola*. The three medium sized producers are FEMSA Cerveza, Grupo Schincariol whose main brand is *Nova Schin* and Cervejaria Petropolis whose main brand is *Itaipava*. FEMSA Cerveza's sales in the Brazilian market depend on its ability to compete with local brewers. Historically, beer imports have not been a significant factor in the Brazilian beer market.

#### ***Demographics of beer drinking population***

We estimate that annual per capita beer consumption for the total Brazilian population reached approximately 50 liters in 2006. The legal drinking age is 18 in Brazil. We consider the population segment of men between the ages of 18 and 45 to be FEMSA Cerveza's primary market. At least 37% of the Brazilian population is under the age of 18 and, therefore, is not considered to be part of the beer drinking population.

Based on historical trends and what management perceives as the continued social acceptance of beer consumption, FEMSA Cerveza believes that general population growth will result in an increase in the number of beer consumers in Brazil. Based on historical trends as measured by the *Instituto Brasileiro de Geografia e Estatística* (Brazilian Institute of Statistics), or IBGE, we expect the Brazilian population to grow at an average annual rate of approximately 1.3% per year over the period from 2007 to 2011. We estimate that over the next 10 years approximately in excess of 2 million additional people per year will become potential beer consumers due to the natural aging of the Brazilian population.

**Table of Contents****Product Overview**

As of December 31, 2006, in Brazil FEMSA Cerveza produced and/or distributed 13 brands of beer in 12 different presentations resulting in a portfolio of 75 different product offerings. The most important brands in FEMSA Cerveza's Brazilian portfolio include: *Kaiser*, *Bavaria*, *Sol*, *Heineken* and *Xingu*. These five brands, all of which are distributed nationwide in Brazil, accounted for approximately 93% of FEMSA Cerveza's Brazil beer sales volume in 2006.

**Beer Presentations**

In its Brazilian breweries, FEMSA Cerveza produces and distributes beer in returnable glass bottles and kegs and in non-returnable aluminum cans and glass bottles. FEMSA Cerveza uses the term presentation to reflect these packaging options. The following table shows the percent of beer sales volume by presentation for the year ended December 31, 2006:

**FEMSA Cerveza's Beer Volume by Presentation, Brazilian breweries****Year Ended December 31, 2006**

<b>Presentation</b>	<b>Percentage</b>
Returnable bottles	55.2%
Non-returnable presentations	44.8
<b>Total</b>	<b>100.0%</b>

**Primary Distribution**

FEMSA Cerveza's primary distribution in Brazil is from its production facilities to the warehouses of the various Coca-Cola franchise bottlers in Brazil. There are 18 Coca-Cola bottlers across Brazil, including subsidiaries of Coca-Cola FEMSA, each responsible for a certain geographic territory.

**Retail Sales and Distribution**

FEMSA Cerveza relies on the 18 different bottlers of the Coca-Cola system across Brazil for the sale and secondary distribution of our beers. The bottlers leverage their infrastructure, sales force, expertise, distribution assets and refrigeration equipment at the point of sale to offer a broad portfolio of products to the retailer.

**Plants and Facilities**

FEMSA Cerveza currently operates eight breweries in Brazil with an aggregate monthly production capacity of 1.7 million hectoliters, equivalent to approximately 19.8 million hectoliters of annual capacity. Six of FEMSA Cerveza's eight Brazilian breweries have received ISO 9002 certifications. A key consideration in the selection of a site for a brewery is its proximity to potential markets, as the cost of transportation is a critical component of the overall cost of beer to the consumer. FEMSA Cerveza's Brazilian breweries are strategically located across the country, as shown in the table below, to better serve FEMSA Cerveza's distribution system.

**Table of Contents****FEMSA Cerveza Facility Allocation in Brazil**

as of December 31, 2006

**FEMSA Cerveza Facility Capacity Summary in Brazil**

Year Ended December 31, 2006

	Average
	Annualized Capacity (in thousands of hectoliters)
<b>Brewery</b>	
Jacareí	7,800
Ponta Grossa	3,200
Araraquara	2,800
Feira de Santana	2,000
Pacatuba	1,600
Gravataí	1,700
Cuiabá	400
Manaus	300
<b>Total</b>	<b>19,800</b>
Average capacity utilization	47.8%

**Exports**

FEMSA Cerveza's principal export market is the United States and its export strategy focuses on that country. In particular, FEMSA Cerveza concentrates efforts on its core markets located in the sun-belt states bordering Mexico, while seeking to develop its brands in key imported beer markets located in the eastern United States. FEMSA Cerveza believes that these two regions of the United States represent its greatest potential market outside of Mexico.



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Prior to January 1, 2005, Labatt USA was the importer of FEMSA Cerveza's brands in the United States. On June 21, 2004, FEMSA Cerveza and two of its subsidiaries entered into distributor and sublicense agreements with Heineken USA. In accordance with these agreements, on January 1, 2005, Heineken USA became the exclusive importer, marketer and seller of FEMSA Cerveza's brands in the United States. These agreements will expire on December 31, 2007. In addition, in April 2007 FEMSA Cerveza and Heineken USA entered into a new ten-year agreement pursuant to which Heineken USA will continue to be the exclusive importer, marketer and distributor of FEMSA Cerveza's beer brands in the United States through 2017.

Export beer sales volume of 2.811 million hectoliters in 2006 represented 7.4% of FEMSA Cerveza's total beer sales volume and accounted for 8.1% of FEMSA Cerveza's total beer sales. The following table highlights FEMSA Cerveza's export beer sales volumes and export beer sales:

**FEMSA Cerveza Export Summary**

	Year Ended December 31,				
	2006	2005	2004	2003	2002
Export beer sales volume <sup>(1)</sup>	2,811	2,438	2,240	1,982	1,955
Volume growth <sup>(2)</sup>	15.3%	8.8%	13.0%	1.4%	6.1%
Percent of total beer sales volumes <sup>(3)</sup>	7.4%	9.0%	8.7%	8.1%	8.2%
Mexican pesos <sup>(4)</sup> (millions)	2,869	2,515	1,860	1,609	1,441
U.S. dollars <sup>(5)</sup> (millions)	256	227	156	133	127
Revenue growth (US\$) <sup>(2)</sup>	13.0%	45.8%	16.7%	4.6%	3.7%
Percent of total beer sales	8.1%	10.2%	8.1%	7.2%	6.5%

Source: FEMSA Cerveza.

(1) Thousands of hectoliters.

(2) Percentage change over prior year.

(3) Reflects Brazilian operations in 2006.

(4) Constant Mexican pesos at December 31, 2006.

(5) Export beer sales are invoiced and collected in U.S. dollars.

FEMSA Cerveza currently exports its products to more than 50 countries. The principal export markets for FEMSA Cerveza are North America, Europe, Latin America and Asia. In 2006, export beer sales volume to these regions accounted for 90.5%, 4.2%, 3.4% and 1.9%, respectively, of FEMSA Cerveza's export beer sales volume.

FEMSA Cerveza's principal export brands are *Tecate*, *XX Lager*, *Dos Equis (Amber)* and *Sol*. These brands collectively accounted for 94% of FEMSA Cerveza's export sales volume for the year ended December 31, 2006.

**FEMSA Comercio****Overview and Background**

FEMSA Comercio operates the largest chain of convenience stores in Mexico, measured in terms of number of stores as of December 31, 2006, under the trade name Oxxo. As of December 31, 2006, FEMSA Comercio operated 4,847 Oxxo stores located in 29 states of the country, with a

particularly strong presence in the northern part of Mexico.

FEMSA Comercio, the largest single customer of FEMSA Cerveza and of the Coca-Cola system in Mexico, was established by FEMSA in 1978 when two Oxxo stores were opened in Monterrey, one store in Mexico City and another store in Guadalajara. The motivating factor behind FEMSA's entrance into the retail industry was to enhance beer sales through company-owned retail outlets as well as to gather information on customer preferences. In 2006, sales of beer through Oxxo represented 9.9% of FEMSA Cerveza's Mexican beer sales volume as well as approximately 13.5% of FEMSA Comercio's revenues. In 2006, a typical Oxxo store carried 1,828 different store keeping units (SKUs) in 31 main product categories, representing a significant increase in the product offering historically carried by Oxxo stores.

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In recent years, FEMSA Comercio has gained importance as an effective distribution channel for our beverage products, as well as a rapidly growing point of contact with our consumers. Based on the belief that location plays a major role in the long-term success of a retail operation such as a convenience store, as well as a role in our continually improving ability to accelerate and streamline the new-store development process, FEMSA Comercio has focused on a strategy of rapid, profitable growth. FEMSA Comercio opened 582, 668, 675 and 706 net new Oxxo stores in 2003, 2004, 2005 and 2006, respectively. The accelerated expansion yielded total revenue growth of 18.7% to reach Ps. 35,500 million in 2006, while same store sales increased 8.2%, which was considerably higher than the retail industry average. FEMSA Comercio served approximately 1,168 million customers in 2006 compared to 978 million in 2005.

### **Business Strategy**

A fundamental element of FEMSA Comercio's business strategy is to utilize its position in the convenience store market to grow in a cost-effective and profitable manner. As a market leader in convenience store retailing, based on internal company surveys, management believes that FEMSA Comercio has an in-depth understanding of its markets and significant expertise in operating a national store chain. FEMSA Comercio intends to continue increasing its store base while capitalizing on the market knowledge gained at existing stores.

FEMSA Comercio has developed proprietary models to assist in identifying appropriate store locations, store formats and product categories. Its model utilizes location-specific demographic data and FEMSA Comercio's experience in similar locations to fine tune the store format and product offerings to the target market. Market segmentation is becoming an important strategic tool, and it should increasingly allow FEMSA Comercio to improve the operating efficiency of each location and the overall profitability of the chain.

FEMSA Comercio has made and will continue to make significant investments in information technology to improve its ability to capture customer information from its existing stores and to improve its overall operating performance. All products carried through Oxxo stores are bar-coded, and all Oxxo stores are equipped with point-of-sale systems that are integrated into a company-wide computer network. To implement revenue management strategies, FEMSA Comercio created a division in charge of product category management for products, such as beverages, fast food and perishables, to enhance and better utilize its consumer information base and market intelligence capabilities. FEMSA Comercio is implementing an ERP system, which will allow FEMSA Comercio to redesign its key operating processes and enhance the usefulness of its market information going forward.

FEMSA Comercio has adopted innovative promotional strategies in order to increase store traffic and sales. In particular, FEMSA Comercio sells high-frequency items such as beverages, snacks and cigarettes at competitive prices. FEMSA Comercio's ability to implement this strategy profitably is partly attributable to the size of the Oxxo chain, as FEMSA Comercio is able to work together with its suppliers to implement their revenue-management strategies through differentiated promotions. Oxxo's national and local marketing and promotional strategies are an effective revenue driver and a means of reaching new segments of the population while strengthening the *Oxxo* brand. For example, the organization has refined its expertise in executing cross promotions (discounts on multi-packs or sales of complementary products at a special price) and targeted promotions to attract new customer segments, such as housewives, by expanding the offerings in the grocery product category in certain stores.

### **Store Locations**

With 4,847 Oxxo stores in Mexico as of December 31, 2006, FEMSA Comercio operates the largest convenience store chain in Latin America measured by number of stores. Oxxo stores are concentrated in the northern part of Mexico, but also have a growing presence in central Mexico and the Gulf coast.

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FEMSA Comercio has aggressively expanded its number of stores over the past several years. The average investment required to open a new store varies, depending on location and format and whether the store is opened in an existing retail location or requires construction of a new store. FEMSA Comercio is generally able to use supplier credit to fund the initial inventory of new stores.

**Growth in Total Oxxo Stores**

	<b>Year Ended December 31,</b>				
	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>	<b>2002</b>
Total Oxxo stores	4,847	4,141	3,466	2,798	2,216
Store growth (% change over previous year)	17.0%	19.5%	23.9%	26.3%	24.6%

FEMSA Comercio currently expects to continue the growth trend established over the past several years by emphasizing growth in areas of high economic potential in existing markets and by expanding in underserved and unexploited markets. Management believes that the southeast part of Mexico is particularly underserved by the convenience store industry.

The identification of locations and pre-opening planning in order to optimize the results of new stores are important elements in FEMSA Comercio's growth plan. FEMSA Comercio continuously reviews store performance against certain operating and financial benchmarks to optimize the overall performance of the chain. Stores unable to maintain benchmark standards are generally closed. Between December 31, 2002 and 2006, the total number of Oxxo stores increased by 2,631, which resulted from the opening of 2,716 new stores and the closing of 85 existing stores.

**Table of Contents****Competition**

Oxxo competes in the convenience store segment of the retail market with 7-Eleven, Super Extra, Circle-K and AM/PM, as well as other local convenience stores. The format of these stores is similar to the format of the Oxxo stores. Oxxo competes both for consumers and for new locations for stores and the managers to operate those stores. Based on an internal market survey conducted by FEMSA Comercio, management believes that, as of December 31, 2006, there were approximately 7,856 stores in Mexico that could be considered part of the convenience store segment of the retail market. Oxxo is the largest chain in Mexico, operating more than half of these stores. Furthermore, FEMSA Comercio operates in 29 states and has much broader geographical coverage than any of its competitors in Mexico.

**Market and Store Characteristics***Market Characteristics*

FEMSA Comercio is placing increased emphasis on market segmentation and differentiation of store formats to more appropriately serve the needs of customers on a location-by-location basis. The principal segments include residential neighborhoods, commercial and office locations and stores near schools and universities, along with other types of specialized locations.

Approximately 68% of Oxxo's customers are between the ages of 15 and 35. FEMSA Comercio also segments the market according to demographic criteria, including income level.

*Store Characteristics*

The average size of an Oxxo store is approximately 111 square meters of selling space, excluding space dedicated to refrigeration, storage or parking. The average constructed area of a store is approximately 186 square meters and, when parking areas are included, the average store size increases to approximately 438 square meters.

**FEMSA Comercio Operating Indicators**

	Year Ended December 31,				
	2006	2005	2004	2003	2002
	(percentage increase compared to previous year)				
Total FEMSA Comercio revenues	18.7%	21.8%	24.8%	24.5%	18.2%
Oxxo same-store sales <sup>(1)</sup>	8.2%	8.7%	8.9%	8.2%	6.0%
	(percentage of total)				
Beer-related data:					
Beer sales as % of total store sales	13.5%	13.0%	13.4%	12.8%	13.3%
Oxxo store sales as a % of FEMSA Cerveza's volume	9.9%	8.6%	7.3%	5.4%	4.5%

(1) Same-store sales growth is calculated by comparing the sales of stores for each year that have been in operation for at least 13 months with the sales of those same stores during the previous year.

Beer, telephone cards, soft drinks and cigarettes represent the main product categories for Oxxo stores. FEMSA Comercio has a distribution agreement with FEMSA Cerveza. As a result of this agreement, Oxxo stores only carry beer brands produced and distributed by FEMSA Cerveza. Prior to 2001, Oxxo stores had informal agreements with Coca-Cola bottlers, including Coca-Cola FEMSA's territories in central Mexico, to sell only their products. Since 2001, a limited number of Oxxo stores began selling *Pepsi* products in certain cities in northern Mexico, as part of a defensive competitive strategy.

Approximately 84% of Oxxo stores are operated by independent managers responsible for all aspects of store operations. The managers are commission agents and are not employees of FEMSA Comercio. Each store manager is the legal employer of the store's staff, which typically numbers six people per store. FEMSA Comercio continually invests in on-site operating personnel, with the objective of promoting loyalty, customer-service and low personnel turnover in the stores.



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### *Advertising and Promotion*

FEMSA Comercio's marketing efforts include both specific product promotions and image advertising campaigns. These strategies seek to increase store traffic and sales, and to reinforce the Oxxo name and market position.

FEMSA Comercio manages its advertising on three levels depending on the nature and scope of the specific campaign: local or store-specific, regional and national. Store-specific and regional campaigns are closely monitored to ensure consistency with the overall corporate image of Oxxo stores and to avoid conflicts with national campaigns. FEMSA Comercio primarily uses point of purchase materials, flyers, handbills and print and radio media for promotional campaigns, although television is used occasionally for the introduction of new products and services. The Oxxo chain's image and brand name are presented consistently across all stores, irrespective of location.

### **Inventory and Purchasing**

FEMSA Comercio has placed considerable emphasis on improving operating performance. As part of these efforts, FEMSA Comercio continues to invest in extensive information management systems to improve inventory management. Electronic data collection has enabled FEMSA Comercio to reduce average inventory levels. Inventory replenishment decisions are carried out on a store-by-store basis.

Management believes that the Oxxo chain's scale of operations provides FEMSA Comercio with a competitive advantage in its ability to realize strategic alliances with suppliers. General category offerings are determined on a national level, although purchasing decisions are implemented on a local, regional or national level, depending on the nature of the product category. Given the fragmented nature of the retail industry in Mexico in general, Mexican producers of beer, soft drinks, bread, dairy products, snacks, cigarettes and other high-frequency products have established proprietary distribution systems with extensive direct distribution routes. As a result, approximately 52% of the products carried by the Oxxo chain are delivered directly to the stores by suppliers. Other products with longer shelf lives are distributed to stores by FEMSA Comercio's distribution system, which includes seven regional warehouses located in Monterrey, Mexico City, Guadalajara, Mexicali, Mérida, León and Chihuahua. The distribution centers operate a fleet of approximately 230 trucks that make deliveries to each store approximately every week.

### **Seasonality**

Oxxo stores experience periods of high demand in December, as a result of the holidays, and in July and August, as a result of increased consumption of beer and soft drinks during the hot summer months. The months of November and February are generally the weakest sales months for Oxxo stores. In general, colder weather during these months reduces store traffic and consumption of cold beverages.

### **Other Stores**

FEMSA Comercio also operates other stores under the names Bara, Six and Matador.

### **Other Business Segment**

Our other business segment consists of the following smaller operations that support our core operations:

Our commercial refrigerators, labels and flexible packaging subsidiaries. The refrigeration business produces vertical and horizontal commercial refrigerators for the soft drink, beer and food industries, with an annual capacity of 180,300 units at December 31, 2006. In 2006, this business sold 175,166 refrigeration units, 14% of which were sold to FEMSA Cerveza, 21.1% of which were sold to Coca-Cola FEMSA and the remainder of which were sold to third parties. The labeling and flexible packaging business has its facility in Monterrey with an annual production capacity of 13,500 tons of flexible packaging. In 2006, this business sold 23% of its label sales volume to FEMSA Cerveza, 11% to Coca-Cola FEMSA and 66% to third parties. Management believes that growth at these businesses will continue to reflect the marketing strategies of Coca-Cola FEMSA and FEMSA Cerveza.

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Our logistics services subsidiary provides logistics services to Coca-Cola FEMSA, FEMSA Empaques, the packaging operations of FEMSA Cerveza, FEMSA Comercio and third party clients that either supply or participate directly in the Mexican beverage industry or in other industries. This business provides integrated logistics support for its clients' supply chain, including the management of carriers and other supply chain services.

One of our subsidiaries is the owner of the *Mundet* brands of soft drinks and certain concentrate production equipment, which are licensed to and produced and distributed by Coca-Cola FEMSA.

Our corporate services subsidiary employs all of our corporate staff, including the personnel managing the areas of finance, corporate accounting, taxation, legal, financial and strategic planning, human resources and internal audit. Through this subsidiary, we direct, control, supervise and review the operations of our sub-holding companies. FEMSA Cerveza, FEMSA Comercio and our packaging subsidiaries pay management fees for the services provided to them. In addition, FEMSA Cerveza and Coca-Cola FEMSA have each entered into a services agreement pursuant to which they pay for specific services.

### **Description of Property, Plant and Equipment**

As of December 31, 2006, we owned all of our manufacturing facilities and substantially all of our warehouses and distribution centers. Our properties primarily consisted of production and distribution facilities for our beer and soft drink operations and office space. In addition, FEMSA Comercio owns approximately 12.7% of the Oxxo store locations, while the other stores are located in properties that are rented under long-term lease arrangements with third parties.

The table below sets forth the location, principal use and production area of our production facilities, and the sub-holding company that owns such facilities.



**Table of Contents****Production Facilities of FEMSA**

As of December 31, 2006

Sub-holding Company	Location	Principal Use	Production Area (in thousands of sq. meters)
<b>Coca-Cola FEMSA</b>			
<i>Mexico</i>	San Cristóbal de las Casas, Chiapas	Soft Drink Bottling Plant	45
	Cedro, Distrito Federal	Soft Drink Bottling Plant	18
	Cuautitlán, Estado de México	Soft Drink Bottling Plant	35
	Los Reyes la Paz, Estado de México	Soft Drink Bottling Plant	50
	Toluca, Estado de México	Soft Drink Bottling Plant	242
	Celaya, Guanajuato	Soft Drink Bottling Plant	87
	León, Guanajuato	Soft Drink Bottling Plant	38
	Morelia, Michoacan	Soft Drink Bottling Plant	50
	Juchitán, Oaxaca	Soft Drink Bottling Plant	27
	Ixtacomitán, Tabasco	Soft Drink Bottling Plant	90
	Apizaco, Tlaxcala	Soft Drink Bottling Plant	80
	Coatepec, Veracruz	Soft Drink Bottling Plant	142
<i>Guatemala</i>	Guatemala City	Soft Drink Bottling Plant	46
<i>Nicaragua</i>	Managua	Soft Drink Bottling Plant	60
<i>Costa Rica</i>	San José	Soft Drink Bottling Plant	52
<i>Panama</i>	Panama City	Soft Drink Bottling Plant	29
<i>Colombia</i>	Barranquilla	Soft Drink Bottling Plant	27
	Bogotá	Soft Drink Bottling Plant	84
	Bucaramanga	Soft Drink Bottling Plant	26
	Cali	Soft Drink Bottling Plant	87
	Manantial	Soft Drink Bottling Plant	67
	Medellín	Soft Drink Bottling Plant	45
<i>Venezuela</i>	Antimano	Soft Drink Bottling Plant	14
	Barcelona	Soft Drink Bottling Plant	141
	Maracaibo	Soft Drink Bottling Plant	68
	Valencia	Soft Drink Bottling Plant	100
<i>Brazil</i>	Campo Grande	Soft Drink Bottling Plant	36
	Jundiá	Soft Drink Bottling Plant	191
	Moji das Cruzes	Soft Drink Bottling Plant	95
<i>Argentina</i>	Alcorta	Soft Drink Bottling Plant	73

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Sub-holding Company	Location	Principal Use	Production Area (in thousands of sq. meters)
<b>FEMSA Cerveza</b>			
	Tecate, Baja California Norte	Brewery	586
	Toluca, Estado de México	Brewery	375
	Guadalajara, Jalisco	Brewery	117
	Monterrey, Nuevo León	Brewery	438
	Navojoa, Sonora	Brewery	517
	Orizaba, Veracruz	Brewery	324
	Pachuca, Hidalgo	Malt Plant	31
	San Marcos, Puebla	Malt Plant	110
	Ensenada, Baja California Norte	Beverage Cans	33
	Toluca, Estado de México	Beverage Cans	22
	Monterrey, Nuevo León	Crown Caps and Can Lids	51
	Acayucan, Veracruz	Silica Sand Mine	7
	Nogales, Veracruz	Bottle Decoration	26
	Orizaba, Veracruz	Glass Bottles	23
<b>Brazil</b>			
	Jacareí	Brewery	72
	Ponta Grossa	Brewery	44
	Araraquara	Brewery	38
	Feira de Santana	Brewery	26
	Pacatuba	Brewery	34
	Gravataí	Brewery	23
	Cuiabá	Brewery	20
	Manaus	Brewery	11

**Insurance**

We maintain an all risk insurance policy covering our properties (owned and leased), machinery and equipment and inventories as well as losses due to business interruptions. The policy covers damages caused by natural disaster, including hurricane, hail, earthquake and damages caused by human acts, including explosion, fire, vandalism, riot and losses incurred in connection with goods in transit. In addition, we maintain an all risk liability insurance policy that covers product liability. We purchase our insurance coverage through an insurance broker. The policies are issued by *Allianz México, S.A., Aseguradora*, and the coverage is partially reinsured in the international reinsurance market. We believe that our coverage is consistent with the coverage maintained by similar companies operating in Mexico.

**Capital Expenditures and Divestitures**

Our consolidated capital expenditures for the years ended December 31, 2006, 2005 and 2004 were Ps. 8,888 million, Ps. 7,034 million and Ps. 7,508 million, respectively, and were for the most part financed from cash from operations generated by our subsidiaries. These amounts were invested in the following manner:

	Year Ended December 31,		
	2006	2005	2004
	(in millions of constant Mexican pesos)		
Coca-Cola FEMSA	Ps. 2,615	Ps. 2,219	Ps. 2,162
FEMSA Cerveza	4,212	3,086	3,409
FEMSA Comercio	1,873	1,472	1,772
Other	188	257	165
<b>Total</b>	<b>Ps. 8,888</b>	<b>Ps. 7,034</b>	<b>Ps. 7,508</b>

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### **Coca-Cola FEMSA**

During 2006, Coca-Cola FEMSA's capital expenditures focused on integration of its acquired territories, placing refrigeration equipment with retailers and investments in returnable bottles and cases, increasing plant operating efficiencies, improving the efficiency of its distribution infrastructure and advancing information technology. Capital expenditures in Mexico were approximately Ps. 1,466 million and accounted for most of its capital expenditures.

#### **FEMSA Cerveza**

##### *Production*

During 2006, FEMSA Cerveza invested approximately Ps. 519 million on equipment substitution and upgrades in its facilities. FEMSA Cerveza's monthly installed capacity as of December 31, 2006 was 2.8 million hectoliters, equivalent to an annualized installed capacity of 33.7 million hectoliters. In addition, FEMSA Cerveza invested Ps. 625 million in plant improvements and equipment upgrades for its beverage can and glass bottle operations.

##### *Distribution*

In 2006, FEMSA Cerveza invested Ps. 506 million in its distribution network. Approximately Ps. 216 million of this amount was invested in the replacement of trucks in its distribution fleet, Ps. 175 million in land and buildings and improvements to leased properties dedicated to various distribution functions, and the remaining Ps. 115 million in other distribution-related investments.

##### *Market-related Investments*

During 2006, FEMSA Cerveza invested approximately Ps. 2,385 million in market-related activities and brand support in the domestic market. Approximately 60% of these investments were directed to customer agreements with retailers and commercial support to owned and third party distributors. Investments in retail agreements with tied customers that exceed a one-year term are capitalized and amortized over the life of the agreement. In general, FEMSA Cerveza's retail agreements are for a period of three to four years. Other market-related investments include the purchase of refrigeration equipment, coolers, plastic furniture and other promotional items. These items are placed with retailers as a means of facilitating the retailers' ability to service consumers and to promote the image and profile of FEMSA Cerveza's brands.

##### *Information Technology Investments*

In addition, during 2006, FEMSA Cerveza invested Ps. 177 million in ERP and other system software projects.

### **FEMSA Comercio**

FEMSA Comercio's principal investment activity is the construction and opening of new stores. During 2006, FEMSA Comercio opened 706 net new Oxxo stores. FEMSA Comercio invested Ps. 1,839 million in 2006 in the addition of new stores and improvements to leased properties.

### **Regulatory Matters**

#### **Competition Legislation**

The *Ley Federal de Competencia Económica* (the Federal Economic Competition Law or the Mexican Competition Law) became effective on June 22, 1993. The Mexican Competition Law and the *Reglamento de la Ley Federal de Competencia Económica* (the Regulations under the Mexican Competition Law), effective as of March 9, 1998, regulate monopolies and monopolistic practices and require Mexican government approval of certain mergers and acquisitions. The Mexican Competition Law subjects the activities of certain Mexican companies, including us, to regulatory scrutiny. In addition, the Regulations under the Mexican Competition Law prohibit members of any trade association from reaching any agreement relating to the price of their products. Management believes that we are currently in compliance in all material respects with Mexican competition legislation.

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In Mexico and in some of the other countries in which we operate, we are involved in different ongoing competition related proceedings. We believe that the outcome of these proceedings will not have a material adverse effect on our financial position or results of operations. See Item 8. Financial Information Legal Proceedings Coca-Cola FEMSA Antitrust Matters and Item 8. Financial Information Legal Proceedings FEMSA Cerveza Antitrust Matters.

### **Environmental Matters**

In all of the countries where we operate, our businesses are subject to federal and state laws and regulations relating to the protection of the environment.

#### *Mexico*

In Mexico, the principal legislation is the *Ley General de Equilibrio Ecológico y Protección al Ambiente* (the Federal General Law for Ecological Equilibrium and Environmental Protection) or the Mexican Environmental Law and the *Ley General para la Prevención y Gestión Integral de los Residuos* (the General Law for the Prevention and Integral Management of Waste), which are enforced by the *Secretaría del Medio Ambiente, Recursos Naturales y Pesca* (the Ministry of the Environment, Natural Resources and Fisheries) or SEMARNAP. SEMARNAP can bring administrative and criminal proceedings against companies that violate environmental laws, and it also has the power to close non-complying facilities. Under the Mexican Environmental Law, rules have been promulgated concerning water, air and noise pollution and hazardous substances. In particular, Mexican environmental laws and regulations require that we file periodic reports with respect to air and water emissions and hazardous wastes and set forth standards for waste water discharge that apply to our operations. We are also subject to certain minimal restrictions on the operation of delivery trucks in Mexico City. We have implemented several programs designed to facilitate compliance with air, waste, noise and energy standards established by current Mexican federal and state environmental laws, including a program that installs catalytic converters and liquid petroleum gas in delivery trucks for our operations in Mexico City. See Coca-Cola FEMSA Product Distribution.

In addition, we are subject to the *Ley Federal de Derechos* (the Federal Law of Governmental Fees), also enforced by SEMARNAP. Adopted in January 1993, the law provides that plants located in Mexico City that use deep water wells to supply their water requirements must pay a fee to the city for the discharge of residual waste water to drainage. In 1995, municipal authorities began to test the quality of the waste water discharge and charge plants an additional fee for measurements that exceed certain standards published by SEMARNAP. All of our bottler plants located in Mexico City, as well as the Toluca plant, met these new standards as of 2001, and as a result, we were not subject to additional fees.

In 2004, Coca-Cola FEMSA built a plastic recycling plant in partnership with The Coca-Cola Company and ALPLA, which manufactures plastic bottles for Coca-Cola FEMSA in Mexico. This plant, which started operations in March 2005, is located in Toluca, Mexico, and has a recycling capacity of 15,000 metric tons per year.

#### *Central America*

Coca-Cola FEMSA's Central American operations are subject to several federal and state laws and regulations relating to the protection of the environment, which have been enacted in the last ten years, as awareness has increased in this region about the protection of the environment and the disposal of dangerous and toxic materials. In some countries in Central America, Coca-Cola FEMSA is in the process of bringing its operations into compliance with new environmental laws. Also, Coca-Cola FEMSA's Costa Rica operations have participated in a joint effort along with the local division of The Coca-Cola Company called *Proyecto Planeta* (Project Planet) for the collection and recycling of non-returnable plastic bottles.

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### *Colombia*

Coca-Cola FEMSA's Colombian operations are subject to several Colombian federal, state and municipal laws and regulations related to the protection of the environment and the disposal of toxic and dangerous materials. These laws include the control of atmospheric emissions and strict limitations on the use of chlorofluorocarbons. Coca-Cola FEMSA is also engaged in nationwide campaigns for the collection and recycling of glass and plastic bottles.

### *Venezuela*

Coca-Cola FEMSA's Venezuelan operations are subject to several Venezuelan federal, state and municipal laws and regulations related to the protection of the environment. The most relevant of these laws are the *Ley Orgánica del Ambiente* (the Organic Environmental Law), the *Ley Sobre Sustancias, Materiales y Desechos Peligrosos* (the Substance, Material and Dangerous Waste Law) and the *Ley Penal del Ambiente* (the Criminal Environment Law). Since the enactment of the Organic Environmental Law in 1995, Coca-Cola FEMSA's Venezuelan subsidiaries have presented to the proper authorities plans to bring their production facilities and distribution centers into compliance with the law. While the laws provide certain grace periods for compliance with the new environmental standards, Coca-Cola FEMSA has had to adjust some of the originally proposed timelines presented to the authorities because of delays in the completion of some of these projects.

### *Brazil*

Coca-Cola FEMSA's Brazilian operations are subject to several federal, state and municipal laws and regulations related to the protection of the environment. Among the most relevant laws and regulations are those dealing with the emission of toxic and dangerous gases and disposal of waste water, which impose penalties, such as fines, facility closures or criminal charges depending upon the level of non-compliance. Coca-Cola FEMSA's production plant located in Jundiaí has been recognized by the Brazilian authorities for its compliance with environmental regulations and for having standards well above those imposed by the law. The plant has been certified for the ISO 9000 since March 1995 and the ISO 14001 since March 1997.

### *Argentina*

Coca-Cola FEMSA's Argentine operations are subject to federal and provincial laws and regulations relating to the protection of the environment. The most significant of these are regulations concerning waste water discharge, which are enforced by the *Secretaría de Recursos Naturales y Ambiente Humano* (the Ministry of Natural Resources and Human Environment) and the *Secretaría de Política Ambiental* (the Ministry of Environmental Policy) for the province of Buenos Aires. Coca-Cola FEMSA's Alcorta plant meets and is in compliance with waste water discharge standards.

We have expended, and may be required to expend in the future, funds for compliance with and remediation under local environmental laws and regulations. Currently, we do not believe that such costs will have a material adverse effect on our results of operations, financial condition or cash flows. However, since environmental laws and regulations and their enforcement are becoming increasingly more stringent in our territories, and there is increased awareness of local authorities for higher environmental standards in the countries where we operate, changes in current regulations may result in an increase in costs, which may have an adverse effect on our future results of operations or financial condition. Management is not aware of any pending regulatory changes that would require a significant amount of additional remedial capital expenditures.

### **Water Supply Law**

FEMSA Cerveza and Coca-Cola FEMSA purchase water in Mexico directly from municipal water companies and pump water from their own wells pursuant to concessions obtained from the Mexican government on a plant-by-plant basis. Water use in Mexico is regulated primarily by the *Ley de Aguas Nacionales de 1992* (the 1992 Water Law), and regulations issued thereunder, which created the *Comisión Nacional del Agua* (the National Water Commission). The National Water Commission is charged with overseeing the national system of water use. Under the 1992 Water Law, concessions for the use of a specific volume of ground or surface water

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generally run for five, ten, fifteen and up to thirty-year terms, depending on the supply of groundwater in each region as projected by the National Water Commission. Concessionaires may request concession terms to be extended upon termination, which is a regular practice. These extensions are given for the same period of time given in the original concession. The Mexican government is authorized to reduce the volume of ground or surface water granted for use by a concession by whatever volume of water is not used by the concessionaire for three consecutive years. However, because the current concessions for each of FEMSA Cerveza and Coca-Cola FEMSA's plants in Mexico do not match each plant's projected needs for water in future years, we successfully negotiated with the Mexican government the right to transfer the unused volume under concessions from certain plants to other plants anticipating greater water usage in the future. These concessions may be terminated if, among other things, we use more water than permitted or we fail to pay required concession-related fees without curing such violations in a timely manner. We believe that we are in compliance with the terms of our existing concessions.

Although we have not undertaken independent studies to confirm the sufficiency of the existing or future groundwater supply, we believe that our existing concessions satisfy our current water requirements in Mexico. We can give no assurances, however, that groundwater will be available in sufficient quantities to meet our future production needs or that we will be able to maintain our current concessions.

We do not currently require a permit to obtain water in our other territories. In Nicaragua, Costa Rica and some plants in Colombia, we own private water wells. In the remainder of our territories, we obtain water from governmental agencies or municipalities. We can give no assurances that water will be available in sufficient quantities to meet our future production needs or that additional regulations relating to water use will not be adopted in the future.

### **ITEM 4A. UNRESOLVED STAFF COMMENTS**

None

### **ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS**

The following discussion should be read in conjunction with, and is entirely qualified by reference to, our audited consolidated financial statements and the notes to those financial statements. Our audited consolidated financial statements were prepared in accordance with Mexican Financial Reporting Standards, which differ in certain significant respects from U.S. GAAP. Notes 27 and 28 to our audited consolidated financial statements provide a description of the principal differences between Mexican Financial Reporting Standards and U.S. GAAP as they relate to us, as well as U.S. GAAP consolidated balance sheets, statements of income, changes in stockholders' equity and cash flows for the same periods presented for Mexican Financial Reporting Standards purposes and a reconciliation to U.S. GAAP of net income and stockholders' equity. See U.S. GAAP Reconciliation.

#### **Overview of Events, Trends and Uncertainties**

Management currently considers the following events, trends and uncertainties to be important to understanding its results of operations and financial position during the periods discussed in this section:

While Coca-Cola FEMSA's Mexican operations continue growing at a steady but moderate pace, operations in Central and South America are growing at accelerated rates. The *Coca-Cola* brand continues to deliver the majority of volume growth. However, the rising price of sweeteners represents uncertainty for our soft drink business generally.

At FEMSA Cerveza, total beer sales volumes have increased in Mexico, Brazil and in the export market. The high price of raw materials, particularly aluminum and barley, represent an uncertainty in our cost structure. Heineken USA has been distributing FEMSA Cerveza's beer brands in the United States since January 1, 2005 with very encouraging results, and we have signed a new agreement that extends this commercial relationship until December 2017.

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FEMSA Comercio continues to increase the number of Oxxo stores and to grow in terms of total revenues and as a percentage of our consolidated total revenues. FEMSA Comercio has lower operating margins than our beverage businesses. We expect to continue to expand the Oxxo chain during 2007.

Our results of operations and financial position are affected by the economic and market conditions in the countries where our subsidiaries conduct their operations, particularly in Mexico. Changes in these conditions are influenced by a number of factors, including those discussed in Item 3. Key Information Risk Factors.

## **Recent Developments**

### ***FEMSA Stock Split***

At our annual general ordinary shareholders meeting held on March 29 2007, our shareholders approved a three-for-one stock split in respect all of our outstanding capital stock. Following the stock split, our total capital stock consists of 2,161,177,770 BD Units and 1,417,048,500 B Units. Our stock split also resulted in a three-for-one stock split our ADSs. The stock-split was conducted on a pro-rata basis in respect of all holders of our shares and all ADSs holders of record as of May 25, 2007, and the ratio of voting and non-voting shares was maintained, thereby preserving our ownership structure as it was prior to the stock-split.

### ***Acquisition of shares of Coca-Cola FEMSA***

On November 3, 2006, we acquired from certain subsidiaries of The Coca-Cola Company 148,000,000 Series D Shares of Coca-Cola FEMSA through our subsidiary CIBSA, representing 8.02% of the total outstanding stock of Coca-Cola FEMSA. We acquired these shares at a price of US\$ 2.888 per share, or US\$ 427.4 million in the aggregate, pursuant to the Memorandum of Understanding with The Coca-Cola Company entered into in connection with the Panamco acquisition. Following the acquisition, and as of May 31, 2007, we hold 53.73% of the total outstanding stock and 63.0% of the voting stock of Coca-Cola FEMSA in the form of Series A shares, The Coca-Cola Company holds 31.60% of the total outstanding stock and 37.0% of its voting stock in the form of Series D shares, and the public float remains unchanged with 14.67% of the total outstanding stock and no voting rights.

### ***FEMSA Cerveza and Heineken USA Import Agreement for United States***

On April 26, 2007, FEMSA Cerveza signed a new agreement with Heineken USA that will effectively extend its previously-existing 3-year import relationship with Heineken USA for an additional 10-year period. Pursuant to the new agreement, Heineken USA will continue to be the sole and exclusive importer, marketer and seller of the FEMSA Cerveza beer brands *Dos Equis*, *Tecate*, *Tecate Light*, *Sol*, *Bohemia* and *Carta Blanca* in the United States. This new agreement will become effective January 1, 2008, immediately following the expiration of the previous 3-year agreement with Heineken USA, and will remain in effect through December 31, 2017. The agreement seeks to expand FEMSA Cerveza's volume growth and brand development, in part through increased marketing investment. Under the terms of the agreement, FEMSA Cerveza will receive a payment for granting Heineken USA exclusive distribution rights in the United States. Heineken in turn will receive an increased share of profitability.

### **Comparability of Information Presented-Panamco Acquisition**

Under Mexican Financial Reporting Standards, Panamco is included in our audited consolidated financial statements since May 2003 and is not included prior to this date. As a result, our consolidated financial information for the year ended December 31, 2003 is not comparable to subsequent periods. The acquisition of Panamco only impacts the comparability of our consolidated information and of the Coca-Cola FEMSA segment. The comparability of our remaining segments is not affected by the acquisition.

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### **Effects of Changes in Economic Conditions**

Our results of operations are affected by changes in economic conditions in Mexico and in the other countries in which we operate. For the years ended December 31, 2006, 2005 and 2004, 78.0%, 82.0% and 80.0%, respectively, of our total sales were attributable to Mexico. After the acquisitions of Panamco and Kaiser, we have greater exposure to countries in which we have not historically conducted operations, particularly countries in Central America, Colombia, Venezuela and Brazil, although we continue to generate a substantial portion of our total sales from Mexico. The participation of these other countries as a percentage of our total sales may increase in future periods, in particular, as Kaiser is included in our consolidated financial information as of January 2006.

Our future results may be significantly affected by the general economic and financial positions in the countries where we operate, including by levels of economic growth, by the devaluation of the local currency, by inflation and high interest rates or by political developments, and may result in lower demand for our products, lower real pricing or a shift to lower margin products. Because a large percentage of our costs are fixed costs, we may not be able to reduce costs and expenses, and our profit margins may suffer as a result of downturns in the economy of each country. In addition, an increase in interest rates in Mexico would increase our cost of Mexican peso-denominated variable interest rate indebtedness and would have an adverse effect on our financial position and results of operations. A depreciation of the Mexican peso relative to the U.S. dollar would increase our cost of those raw materials, the price of which is paid in or determined with reference to the U.S. dollar, and our debt obligations denominated in U.S. dollars, and thereby may negatively affect our financial position and results of operations.

### **Operating Leverage**

Companies with structural characteristics that result in margin expansion in excess of sales growth are referred to as having high operating leverage.

The operating subsidiaries of Coca-Cola FEMSA and FEMSA Cerveza are engaged, to varying degrees, in capital-intensive activities. The high utilization of the installed capacity of the production facilities results in better fixed cost absorption, as increased output results in higher revenues without additional fixed costs. Absent significant increases in variable costs, gross profit margins will expand when production facilities are operated at higher utilization rates. Alternatively, higher fixed costs will result in lower gross profit margins in periods of lower output.

In addition, the commercial operations of Coca-Cola FEMSA and FEMSA Cerveza are carried out through extensive distribution networks, the principal fixed assets of which are warehouses and trucks. The distribution systems of both Coca-Cola FEMSA and FEMSA Cerveza are designed to handle large volumes of beverages. Fixed costs represent an important proportion of the total distribution expense of both Coca-Cola FEMSA and FEMSA Cerveza. Generally, the higher the volume that passes through the distribution system, the lower the fixed distribution cost as a percentage of the corresponding revenues. As a result, operating margins improve when the distribution capacity is operated at higher utilization rates. Alternatively, periods of decreased utilization because of lower volumes will negatively affect our operating margins.

### **Critical Accounting Estimates**

The preparation of our audited consolidated financial statements requires that we make estimates and assumptions that affect (1) the reported amounts of our assets and liabilities, (2) the disclosure of our contingent liabilities at the date of the financial statements and (3) the reported amounts of revenues and expenses during the reporting period. We base our estimates and judgments on our historical experience and on various other reasonable factors that together form the basis for making judgments about the carrying values of our assets and liabilities. Our actual results may differ from these estimates under different assumptions or conditions. We evaluate our estimates and judgments on an on-going basis. Our significant accounting policies are described in note 4 to our audited consolidated financial statements. We believe our most critical accounting policies that imply the application of estimates and/or judgments are the following:



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### *Allowance for doubtful accounts*

We determine our allowance for doubtful accounts based on an evaluation of the aging of our receivable portfolio. The amount of the allowance considers our historical loss rate on receivables and the economic environment in which we operate. Our beer operations represent the most important part of the consolidated allowance for doubtful accounts as a result of the credit that FEMSA Cerveza extends to retailers, on terms and conditions in accordance with industry practices. Coca-Cola FEMSA and FEMSA Comercio sales are generally realized in cash.

### *Bottles and cases; allowance for bottle breakage*

Returnable bottles and cases are recorded at acquisition cost and restated to their replacement cost. For the year ended December 31, 2005, FEMSA Cerveza classified returnable bottles and cases as inventory. Beginning on January 1, 2006, FEMSA Cerveza classifies bottles and cases as long-lived assets in accordance with their estimated useful lives. For FEMSA Cerveza and Coca-Cola FEMSA, breakage is expensed as incurred, and returnable bottles and cases are not depreciated. Whenever we decide to discontinue a particular returnable presentation and retire it from the market, we write-off the discontinued presentation through an increase in the breakage expense. We determine depreciation of bottles and cases only for tax purposes. FEMSA Cerveza beginning in 2005 for tax purposes, classifies bottles and cases as fixed assets and compute depreciation using the straight-line method at an annual rate of 10%. This change in classification did not impact the total amount of taxes payable, but in 2005, it generated surcharges over taxes not paid in prior years.

We periodically compare the carrying value of bottle breakage expense with the calculated depreciation expense of our returnable bottles and cases in plant and distribution centers, estimating a useful life of five years for glass beer bottles, four years for returnable glass soft drink bottles and plastic cases and one year for returnable plastic bottles. These useful lives are determined in accordance with our business experience. The annual calculated depreciation expense has been similar to the annual carrying value of bottle breakage expense. Whenever we decide to discontinue a particular returnable presentation and retire it from the market, we write off the discontinued presentation through an increase in breakage expense.

### *Property, plant and equipment*

Property, plant and equipment are depreciated over their estimated useful lives. The estimated useful lives represent the period we expect the assets to remain in service and to generate revenues. We base our estimates on independent appraisals and the experience of our technical personnel.

We describe the methodology used to restate imported equipment in note 4 (g) to our audited consolidated financial statements, which includes applying the exchange and inflation rates of the country of origin utilized as permitted by Mexican Financial Reporting Standards. We believe this method more accurately presents the fair value of the assets than restated cost determined by applying inflation factors.

We valued at fair value all fixed assets acquired, considering their operating conditions and the future cash flows expected to be generated based on their estimated remaining useful life as determined by management.

During 2005, we began to re-examine our refrigeration equipment for accounting purposes and to evaluate its general functionality. Our examination focused mainly on electrical functioning, maintenance, reliability of internal controls over this equipment and supplier confirmations regarding physical conditions and the estimated remaining useful life of the equipment. Based on our experience, and our research regarding maintenance concerns and replacement plans for refrigeration equipment in general, we determined that we should increase the accounting estimate regarding the useful lives of Coca-Cola FEMSA's refrigeration equipment used in its Mexican operations from five to seven years. This change was accounted for prospectively and led to a reduction in our depreciation expense of Ps. 127 million recognized in our 2006 consolidated results of operations. We are still examining refrigeration equipment in the remaining Coca-Cola FEMSA territories based on the same considerations used to evaluate the Mexican operations, and we expect to complete this project during 2007.

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### *Valuation of intangible assets and goodwill*

We identify all intangible assets to reduce as much as possible the goodwill associated with business acquisitions. We separate intangible assets between those with a finite useful life and those with an indefinite useful life, in accordance with the period over which we expect to receive the benefits.

We determine the fair value of assets acquired and liabilities assumed as of the date of acquisition, and we assigned the excess purchase price over the fair value of the net assets. In certain circumstances this resulted in the recognition of an intangible asset. The intangible assets are subject to annual impairment tests. We have recorded intangible assets with indefinite lives, which consist of:

Coca-Cola FEMSA's rights to produce and distribute *Coca-Cola* trademark products for Ps. 39,399 million as a result of the Panamco acquisition;

Trademarks and distribution rights for Ps. 10,897 million as a result of the acquisition of the 30% interest of FEMSA Cerveza and distribution rights acquired from a third-party distributor;

Trademarks and goodwill as a result of the acquisition of Kaiser for Ps. 3,706 million; and

Other intangible assets with indefinite lives that amounted to Ps. 746 million.

For Mexican Financial Reporting Standards purposes, goodwill is the difference between the price paid and the fair value of the shares and/or net assets acquired that was not assigned directly to an intangible asset. Goodwill is recorded in the functional currency of the subsidiary in which the investment was made and is restated by applying the inflation rate factors of the country of origin and the year-end exchange rate. Until December 31, 2004 under Mexican Financial Reporting Standards, goodwill was amortized using the straight-line method over a period of no more than 20 years. The amount of goodwill amortization in 2004 was Ps. 15 million. In 2005, Bulletin B-7, *Adquisiciones de Negocios* (Business Acquisitions), was issued, which establishes that goodwill is no longer subject to amortization, being subject instead to an annual impairment test.

### *Impairment of goodwill and long-lived assets*

We continually review the carrying value of our goodwill and long-lived assets for impairment. We review for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable based on our estimated discounted future cash flows to be generated by those assets. While we believe that our estimates of future cash flows are reasonable, different assumptions regarding such cash flows could materially affect our evaluations.

Our evaluations during 2006 and up to the date of this annual report did not lead to any impairment of goodwill or long-lived assets. We can give no assurance that our expectations will not change as a result of new information or developments. Future changes in economic or political conditions in any country in which we operate or in the industries in which we participate, however, may cause us to change our current assessment.

### *Executory contracts*

As part of the normal course of business, we frequently invest in the development of our beer distribution channels through a variety of commercial agreements with different retailers in order to generate sales volume. These agreements are considered to be executory contracts and accordingly the costs incurred under these contracts are recognized according to when performance occurs.

These agreements require cash disbursements to be made in advance to certain retailers in order to fund activities intended to generate sales volume. These advance cash disbursements are then compensated for as sales are invoiced. These disbursements are considered to be market-related investments, which are capitalized as other assets. The amortization of amounts capitalized is presented as a reduction of net sales in relation to the volume sold to each retailer. The period of amortization is between three and four years, which is the normal term of the commercial agreements.

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We periodically evaluate the carrying value of executory contracts. If the carrying value is considered to be impaired, these assets are written down as appropriate. The accuracy of the carrying value is based on our ability

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to predict certain key variables such as sales volume, prices and other industry and economic factors. Predicting these key variables involves assumptions based on future events. These assumptions are consistent with our internal projections.

*Labor liabilities*

Our labor liabilities are comprised of pension plans liabilities, seniority premiums, post-retirement medical services and severance indemnities. The determination of our obligations and expenses for pension and other post-retirement benefits is dependent on our determination of certain assumptions used by independent actuaries in calculating such amounts. We evaluate these assumptions at least annually. In 2006, we approved a modification to our pension and retirement plans effective in 2007. Through 2006, our pension and retirement plans provided for lifetime monthly payments as a complement to the pension payment received from the Mexican Social Security Institute (*Instituto Mexicano del Seguro Social* or IMSS). Our modified pension and retirement plans provide for one lump-sum payment in addition to pension received from the IMSS, which will supplement the beneficiary's earnings.

Additionally, in 2006, we modified the long-term assumptions used in the actuarial calculations for Mexican subsidiaries based on changes in the company's revised estimate of current prices for settling its related obligations as a result of recent stability in the Mexican economy. These assumptions are described in note 17 to our consolidated financial statements and include the discount rate, expected long-term rate of return on plan assets and rates of increase in compensation costs. All our assumptions depend on the economic circumstances of each country where we operate.

These changes were accounted for as unrecognized prior service costs and unrecognized actuarial net loss and will be amortized over the expected service period of our personnel. The net effect of the changes mentioned above was an increase in pension and retirement plan, seniority premium and severance indemnity liabilities of Ps.768, Ps.18 and Ps.22 million, respectively.

In accordance with Mexican Financial Reporting Standards, actual results that differ from our assumptions (actuarial gains or losses) are accumulated and amortized over future periods and, therefore, generally affect our recognized expenses and recorded obligations in these future periods. While we believe that our assumptions are appropriate, significant differences in our actual experience or significant changes in our assumptions may materially affect our pension and other post-retirement obligations and our future expense. The following table is a summary of the three key assumptions to be used in determining 2007 annual pension expense, along with the impact on pension expense of a 1% change in each assumed rate.

Assumption	2007 Rate <sup>(1)</sup> (in real terms)	Impact of Rate Change <sup>(2)</sup>	
		+1%	-1%
<b>Mexican and Foreign Subsidiaries:</b>			
Discount rate	4.5%	Ps. (709)	Ps. 556
Salary increase	1.5%	509	(494)
Return on assets	4.5%	(18)	36

(1) Calculated using a measurement dated as of December 2006.

(2) The impact is not the same for an increase of 1% as for a decrease of 1% because the rates are not linear.

*Income taxes*

We recognize deferred tax assets and liabilities based on the differences between the financial statement carrying amounts and the tax basis of assets and liabilities. We regularly review our deferred taxes for recoverability and/or payment, and establish a valuation allowance based on historical taxable income, projected future taxable income and the expected timing of the reversals of existing temporary differences. If these estimates and related assumptions change in the future, we may be required to record additional valuation allowances against our deferred taxes resulting in an impact in net income.

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On December 1, 2004, an amendment to the Mexican income tax law was published and became effective as of January 1, 2005. Under this amendment:

The statutory income tax rate decreased to 30% for 2005 and will be subsequently reduced by one percentage point per year through 2007, when the rate is 28%;

The tax deduction for inventory will be made through cost of sales, and the inventory balance as of December 31, 2004 will be taxable during the next four to twelve years, based on specific criteria provided in the tax regulations;

Paid employee profit sharing will be deductible for income tax purposes; and

The limit on stockholders' participation in taxable income or loss from Mexican subsidiaries will be eliminated for tax consolidation purposes.

Based on this amendment, we adjusted our deferred income tax liability by applying different tax rates than those originally used to temporary differences according to their estimated dates of reversal. This resulted in a decrease of Ps. 647 million in 2004 of our deferred income tax liability and to the related reduction in deferred taxes in our income statement.

### *Tax and legal contingencies*

We are subject to various claims and contingencies related to tax and legal proceedings as described in note 25 to our audited consolidated financial statements. 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 periodically assesses the probability of loss for such contingencies and accrues a liability and/or discloses the relevant circumstances, as appropriate. If the potential loss from any claim or legal proceeding is considered probable and the amount can be reasonably estimated, we accrue a liability for the estimated loss.

### *Derivative Financial Instruments*

As we mention in note 4 (q) to our consolidated financial statements, beginning in 2005 we began to apply Bulletin C-10, *Instrumentos Financieros Derivados y Operaciones de Cobertura* (Derivative Financial Instruments and Hedging Activities), which requires us to measure all derivative financial instruments at fair value and recognize them in the balance sheet as an asset or liability. Changes in the fair value of derivative financial instruments are recorded each year in net income or as a component of cumulative other comprehensive income, based on the type of hedging instrument and the ineffectiveness of the hedge. The fair values of derivative financial instruments are determined considering quoted prices in recognized markets. If such instruments are not traded, fair value is determined by applying techniques based upon technical models supported by sufficient reliable and verifiable data, recognized in the financial sector. We base our forward price curves upon market price quotations.

### **New Accounting Pronouncements**

Other than as described below, we do not anticipate any significant impact on our consolidated balance sheet, results of operations, changes to our financial position or cash flows, as a result of our adoption of the new accounting standards described below.

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*Under Mexican Financial Reporting Standards (Normas de Información Financiera, or NIF)*

### **NIF B-3, *Estado de resultados* (Income Statement)**

NIF B-3 sets the general standards for presenting and structuring the statement of income, the minimum content requirements and general disclosure standards. Consistent with NIF A-5, Basic Elements of Financial Statements, NIF B-3 now classifies revenues, costs and expenses, as ordinary and non-ordinary. Ordinary items (even if infrequent) are delivered from the primary activities representing an entity's main source of revenue. Non-ordinary items are derived from activities other than those representing an entity's main source of revenues. Consequently, the classification of certain transactions as special or extraordinary, according to former Bulletin B-3, which was previously in effect, was eliminated. As part of the structure of the income statement, ordinary items are required to be presented first and, at a minimum, present income or loss before income taxes, income or loss before discontinued operations, if any, and net income or loss. Presenting operating income is neither required nor prohibited by NIF B-3. Cost and expense items may be classified by function, by nature or a combination of both. When classified by function, gross income may be presented. Statutory employee profit sharing should now be presented as an ordinary expense (within other income (expense) pursuant to NIF No. 4 issued in January 2007) and should no longer be presented with income tax. Special items mentioned in particular Mexican Financial Reporting Standards should now be part of other income and expense, and items formerly recognized as extraordinary should be part of non-ordinary items. NIF B-3 is effective for financial periods beginning January 1, 2007.

### **NIF B-13, *Hechos posteriores a la fecha de los estados financieros* (Subsequent Events)**

This standard requires that for (1) asset and liability restructurings and (2) creditor waivers to their right to demand payment in case the entity defaults on contractual obligations, in each case occurring in the period between the date of the financial statements and the date of their issuance, disclosure only needs to be included in a note to the financial statements while recognition of these items should take place in the financial statements for the period in which such event takes place. Previously, these events were recognized in the financial statements in addition to their disclosure. NIF A-7, Presentation and Disclosure, which has been in effect as of January 1, 2006, requires, among other things, that the date on which the issuance of the financial statements is authorized be disclosed as well as for the name of the authorizing management officer(s) or body (bodies) to be disclosed. NIF B-13 establishes that if the entity owners or others are empowered to modify the financial statements, such fact should also be disclosed. Subsequent approval of the financial statements by the stockholders or other body does not change the subsequent period, which ends when issuance of the financial statements is authorized. NIF B-13 is effective for financial periods beginning January 1, 2007.

### **NIF C-13, *Partes relacionadas* (Related Parties)**

This standard broadens the concept of related parties to include (1) the overall business in which the reporting entity participates; (2) close family members of key officers; and (3) any fund created in connection with a labor-related compensation plan. In addition, NIF C-13 requires the following disclosure: (1) that the terms and conditions of consideration paid or received in transactions carried out between related parties are equivalent to those of similar transactions carried out by the reporting entity with independent parties, to the extent sufficient evidence exists as a basis for comparison; (2) any benefits granted to key officers; and (3) the name of the direct controlling company and, if different, name of the ultimate controlling company. Notes to comparative financial statements of prior periods should disclose the new provisions of NIF C-13. NIF C-13 is effective for financial periods beginning January 1, 2007.

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**NIF D-6, *Capitalización del resultado integral de financiamiento* (Capitalization of Integral Result of Financing)**

NIF D-6 establishes general capitalization standards that include specific accounting for financing in domestic and foreign currencies, or a combination of each. Some of these standards include: (1) a provision for the mandatory capitalization of integral result of financing directly attributable to the acquisition of qualifying assets; (2) a clarification that yields obtained from temporary investments before capital expenditures are made must be excluded from the amount capitalized, to the extent financing in domestic currency is used to acquire these assets; (3) a provision specifying that exchange gains or losses from foreign currency financing should be capitalized considering the valuation of associated hedging instruments, if any; (4) a methodology to calculate capitalizable integral result of financing relating to funds from generic financing; (5) a clarification that, in the context of land, integral result of financing may be capitalized if development is being undergone; and (6) the establishment of other conditions that must be met to capitalize integral result of financing, as well as rules indicating when integral of financing should no longer be capitalized. NIF D-6 is effective for financial periods beginning January 1, 2007.

*Under U.S. GAAP*

**Accounting for Certain Hybrid Financial Instruments – an amendment of FASB Statement No. 133 and 140 , or SFAS No. 155**

SFAS No.155 amends SFAS No.133, Accounting for Derivative Instruments and Hedging Activities, and SFAS No.140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. SFAS No. 155 establishes that: (1) fair value re-measurement is permitted for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, (2) interest-only strips and principal-only strips are not subject to SFAS No. 133 requirements, which is a clarification to past pronouncements (3) interests must be evaluated in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation, (4) concentrations of credit risk in the form of subordination are not embedded derivatives, which is a clarification to past pronouncements; (5) the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument is eliminated, which represents a change to SFAS No. 140. SFAS No.155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. We are in the process of determining the impact of adopting this new accounting principle on our consolidated financial position and results of operations.

**Accounting for Servicing of Financial Assets – an amendment of FASB Statement No. 140 , or SFAS No. 156**

SFAS No. 156 amends SFAS No.140 with respect to the accounting for separately recognized servicing assets and servicing liabilities and establishes that entities must recognize servicing assets or servicing liabilities each time they undertake an obligation to service a financial asset by entering into a servicing contract in certain specific situations. SFAS No. 156 also requires recognizing separately servicing assets and servicing liabilities to be initially measured at fair value, if practicable, and also permits an entity to choose either the amortization method or the fair value measurement method to recognize servicing assets and servicing liabilities. SFAS No. 156 is effective as of the beginning of the first fiscal year that begins after September 15, 2006. We are in the process of determining the impact of adopting this new accounting principle on our consolidated financial position and results of operations.

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**Fair Value Measurements , or SFAS No. 157**

SFAS No. 157 establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 also clarifies the definition of exchange price as the price between market participants in an orderly transaction to sell an asset or transfer a liability in the market in which the reporting entity would transact for the asset or liability, that is, the principal or most advantageous market for the asset or liability. The changes to current practice resulting from the application of this statement relate to the definition of fair value, the methods used to measure fair value, and the expanded disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. We are in the process of determining the impact of adopting this new accounting principle on our consolidated financial position and results of operations.

**Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R) , or SFAS No. 158**

SFAS No. 158 requires companies to measure the fair value of its plan assets and benefit obligations as of the date of its year-end balance sheet. Companies no longer are permitted to measure the funded status of their plan(s) by being able to choose a measurement date up to three months prior to year end. This aspect of SFAS No. 158 is effective for all companies in fiscal years ending after December 15, 2008, but does not impact our company, our results of operations or our cash flows, as our measurement date is the same as our fiscal year end. Retrospective application of SFAS No. 158 is not permitted.

**Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109, or SFAS Interpretation ( FIN ) No. 48**

This interpretation provides detailed guidance for financial statement recognition, measurement and disclosure of uncertain tax positions recognized in a company's financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN No. 48 requires a company to recognize the financial statement impact of a tax position when it is more likely than not that the position will be sustained upon examination. If the tax position meets the more-likely-than-not recognition threshold, the tax effect is recognized at the largest amount of the benefit that is greater than 50% likely of being realized upon ultimate settlement. Any difference between the tax position taken in the tax return and the tax position recognized in the financial statements using the criteria above results in the recognition of a liability in the financial statements for the unrecognized benefit. Similarly, if a tax position fails to meet the more-likely-than-not recognition threshold, the benefit taken in the tax return will also result in the recognition of a liability in the financial statements for the full amount of the unrecognized benefit. FIN No. 48 will be effective for fiscal years beginning after December 15, 2006 (including the first interim period for calendar-year companies) and the provisions of FIN No. 48 were applicable with respect to all tax positions under SFAS No. 109 upon initial adoption. The cumulative effect of applying the provisions of this interpretation will be reported as an adjustment to the opening balance of retained earnings for that fiscal year. We are in the process of determining the impact of adopting this new accounting principle on our consolidated financial position and results of operations.

**How Taxes Are Collected from Customers and Remitted to Governmental Authorities Should be Presented in the Income Statement , or Emerging Issues Task Force (EITF) Issue No. 06-3**

The scope of EITF Issue No. 06-3 includes any tax assessed by a governmental authority that is directly imposed on a revenue-producing transaction between a seller and a customer and may include, but is not limited to, sales, use, value added, and certain excise taxes. The Emerging Issues Task Force (EITF) reached a tentative conclusion that the presentation of taxes mentioned above on either a gross (included in revenues and costs) or a net (excluded from revenues) basis is an accounting policy decision that should be disclosed pursuant to Accounting Principles Board (APB) Opinion No. 22. In addition, for any such



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taxes that are reported on a gross basis, a company should disclose the amounts of those taxes in interim and annual financial statements for each period for which an income statement is presented if the amounts are significant. The disclosure of these taxes can be done on an aggregate basis. The tentative conclusion of the EITF requires only the presentation of additional disclosures and, as a result, an entity would not be required to reevaluate its existing policies related to taxes assessed by a governmental authority that are directly imposed on a revenue-producing transaction between a seller and a customer. However, if a company chooses to reevaluate its existing policies and elects to change the presentation of taxes within the scope of EITF Issue No. 06-3, it must follow the requirements of Statement No. 154, Accounting Changes and Error Corrections a replacement of APB Opinion No. 20 and FASB Statement No. 3. The EITF also reached a tentative conclusion that Issue No. 06-3 should be applied to financial reports for interim and annual reporting periods beginning after December 15, 2006. Earlier application is permitted. We are in the process of determining the impact of adopting this new accounting principle on our consolidated financial position and results of operations.

**Operating Results**

The following table sets forth our consolidated income statement under Mexican Financial Reporting Standards for the years ended December 31, 2006, 2005 and 2004:

	Year Ended December 31,			
	2006	2006	2005	2004
	(in millions of U.S. dollars and constant Mexican pesos at December 31, 2006)			
Net sales	\$ 11,667	Ps. 125,994	Ps. 111,051	Ps. 101,637
Other operating revenues	40	433	585	679
<b>Total revenues</b>	<b>11,707</b>	<b>126,427</b>	<b>111,636</b>	<b>102,316</b>
Cost of sales	6,291	67,940	59,483	54,190
Gross profit	5,416	58,487	52,153	48,126
Operating expenses:				
Administrative	778	8,400	7,466	7,245
Selling	3,028	32,697	28,284	25,917
<b>Total operating expenses</b>	<b>3,806</b>	<b>41,097</b>	<b>35,750</b>	<b>33,162</b>
Income from operations	1,610	17,390	16,403	14,964
Interest expense	(374)	(4,040)	(4,520)	(4,076)
Interest income	65	707	684	613
Interest expense, net	(309)	(3,333)	(3,836)	(3,463)
Foreign exchange gain (loss)	(20)	(217)	308	(23)
Gain on monetary position	129	1,395	1,169	2,112
Market value loss on ineffective portion of derivative financial instrument	(10)	(109)	(160)	
Integral result of financing	(210)	(2,264)	(2,519)	(1,374)
Other expenses, net	(104)	(1,125)	(452)	(856)
Income before taxes and employee profit sharing	1,296	14,001	13,432	12,734
Taxes and employee profit sharing	445	4,806	4,866	2,649
<b>Consolidated net income</b>	<b>\$ 851</b>	<b>Ps. 9,195</b>	<b>Ps. 8,566</b>	<b>Ps. 10,085</b>
Net majority income	613	6,622	5,766	6,411
Net minority income	238	2,573	2,800	3,674

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Consolidated net income	\$	851	Ps. 9,195	Ps. 8,566	Ps. 10,085
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The following table sets forth certain operating results by reportable segment under Mexican Financial Reporting Standards for each of our segments for the years ended December 31, 2006, 2005 and 2004:

	Year Ended December 31,			Percentage Growth	
	2006	2005	2004	2006 vs. 2005	2005 vs. 2004
	(in millions of constant Mexican pesos at December 31, 2006, except for percentages)				
<b>Net sales</b>					
Coca-Cola FEMSA	Ps. 57,539	Ps. 53,601	Ps. 50,899	7.3%	5.3%
FEMSA Cerveza	35,370	28,521	26,612	24.0%	7.2%
FEMSA Comercio	35,500	29,898	24,556	18.7%	21.8%
<b>Total revenues</b>					
Coca-Cola FEMSA	57,738	53,997	51,276	6.9%	5.3%
FEMSA Cerveza	35,599	28,690	26,848	24.1%	6.9%
FEMSA Comercio	35,500	29,898	24,556	18.7%	21.8%
<b>Cost of sales</b>					
Coca-Cola FEMSA	30,196	27,522	26,227	9.7%	4.9%
FEMSA Cerveza	15,271	11,564	11,048	32.1%	4.7%
FEMSA Comercio	25,866	21,967	18,037	17.8%	21.8%
<b>Gross profit</b>					
Coca-Cola FEMSA	27,542	26,475	25,049	4.0%	5.7%
FEMSA Cerveza	20,328	17,126	15,800	18.7%	8.4%
FEMSA Comercio	9,634	7,931	6,519	21.5%	21.7%
<b>Income from operations</b>					
Coca-Cola FEMSA	9,456	9,218	8,459	2.6%	9.0%
FEMSA Cerveza	5,915	5,590	5,101	5.8%	9.6%
FEMSA Comercio	1,604	1,310	979	22.4%	33.8%
<b>Depreciation</b>					
Coca-Cola FEMSA <sup>(1)</sup>	2,393	2,385	2,177	0.4%	9.5%
FEMSA Cerveza	1,684	1,558	1,604	8.1%	(2.8)%
FEMSA Comercio	415	336	232	23.8%	44.8%
<b>Gross margin<sup>(2)</sup></b>					
Coca-Cola FEMSA	47.7%	49.0%	48.9%	(1.3)%	0.2%
FEMSA Cerveza	57.1%	59.7%	58.8%	(2.6)%	0.9%
FEMSA Comercio	27.1%	26.5%	26.5%	0.6%	0.0%
<b>Operating margin<sup>(3)</sup></b>					
Coca-Cola FEMSA	16.4%	17.1%	16.5%	(0.7)%	0.6%
FEMSA Cerveza	16.6%	19.5%	19.0%	(2.9)%	0.5%
FEMSA Comercio	4.5%	4.4%	4.0%	0.1%	0.4%

(1) Includes breakage of bottles of Coca-Cola FEMSA.

(2) Gross margin calculated with reference to total revenues.

(3) Operating margin calculated with reference to total revenues.

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**Results of Operations For Year Ended December 31, 2006 Compared to Year Ended December 31, 2005**

**FEMSA Consolidated**

In 2006, FEMSA Cerveza acquired 99.83% of the Brazilian brewer, Cervejarias Kaiser, or Kaiser, through a series of transactions with Molson Coors and Heineken N.V. The following discussion of our consolidated results for 2006 fully reflects the inclusion of the results for Brazilian beer operations in 2006. However, because we did not own Brazilian beer operations prior to this period, our consolidated results and FEMSA Cerveza's results for 2006 are not fully comparable to the prior period.

*Total Revenues*

Consolidated total revenues increased 13.2% to Ps. 126,427 million in 2006 compared to Ps. 111,636 million in 2005. All of FEMSA's operations soft drinks, beer and retail contributed to this revenue growth. FEMSA Cerveza was the largest contributor to consolidated total revenue growth in 2006, representing approximately 47% of the increase, due to the inclusion of its newly acquired Brazilian beer operations and a 9.3% increase in Mexico beer sales, which reached Ps. 25,286 million in 2006. The remaining growth came primarily from FEMSA Comercio and Coca-Cola FEMSA. FEMSA Comercio's total revenues increased 18.7% to Ps. 35,500 million, due in large part to the 706 net new stores opened during the year. Coca-Cola FEMSA's total revenues increased 6.9% to Ps. 57,738 million, mainly due to increased prices and strong volume growth throughout most of its nine countries of operation. This increase was partially offset by Mexico's continued pricing pressure, which was partly compensated for by price improvements in the other areas.

*Gross Profit*

Consolidated cost of sales increased 14.2% to Ps. 67,940 million in 2006 compared to Ps. 59,483 million in 2005. Approximately 79% of this increase resulted from FEMSA Comercio and its Oxxo store expansion, and to FEMSA Cerveza, which increased its cost of sales due to the acquisition of its Brazilian beer operations.

Consolidated gross profit increased 12.1% to Ps. 58,487 million in 2006 compared to Ps. 52,153 million in 2005. Approximately 51% of this increase resulted from FEMSA Cerveza, due to the inclusion of its newly acquired Brazilian operations. Gross margin decreased 0.4 percentage points to 46.3% of consolidated total revenues in 2006, compared to 46.7% of consolidated total revenues in 2005. The slight decline in consolidated gross margin from 2005 levels resulted from the inclusion of FEMSA Cerveza's lower margin beer operations in Brazil, and the increased contribution of FEMSA Comercio in our consolidated financial results, which has lower gross margin relative to our other operations, typical of convenience and retail store formats.

*Income from Operations*

Consolidated operating expenses increased 15.0% to Ps. 41,097 million in 2006 compared to Ps. 35,750 million in 2005. Approximately 54% of this increase was due to FEMSA Cerveza, which increased expenses year-over-year due to the inclusion of its newly acquired Brazilian operations and increased selling expenses in the Mexican market, primarily for advertising and market-related initiatives. As a percentage of total revenues, consolidated operating expenses increase 0.5 percentage points to reach 32.5% in 2006 compared with 32.0% in 2005.

Consolidated administrative expenses increased 12.5% to Ps. 8,400 million in 2006 compared to Ps. 7,466 million in 2005. As a percentage of total revenues, consolidated administrative expenses decreased 0.1 percentage points to reach 6.6% in 2006 compared with 6.7% in 2005. The lower level of administrative expenses relative to total revenue growth resulted from a 0.1% reduction in administrative expenses at Coca-Cola FEMSA and stable administrative expenses as a percentage of total revenues at FEMSA Cerveza (excluding Brazil) and FEMSA Comercio.

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Consolidated selling expenses increased 15.6% to Ps. 32,697 million in 2006 as compared to Ps. 28,284 million in 2005. Approximately 54% of this increase was due to FEMSA Cerveza and the inclusion of its newly acquired Brazilian operations, and 29% to FEMSA Comercio's rapid rate of growth. As a percentage of total beer revenues, selling expenses increased 0.6 percentage points to reach 25.9% in 2006 compared to 25.3% in 2005.

We incur various expenses related to the distribution of our products that are accounted for in our selling expenses. During 2006 and 2005, our distribution costs amounted to Ps. 9,190 million and Ps. 8,586 million, respectively. The exclusion of these charges from our cost of sales may result in the amounts reported as gross profit not being comparable to other companies that may include all expenses related to their distribution network in cost of sales when calculating gross profit or an equivalent measure.

Consolidated income from operations increased 6.0% to Ps. 17,390 million in 2006 as compared to Ps. 16,403 million in 2005. Over one-third of this increase resulted from FEMSA Cerveza and its top-line growth combined with gross margin improvements that offset increased operating expenses and the negative impact from the inclusion of the newly acquired Brazilian operations. The remaining amount is attributable to FEMSA Comercio and Coca-Cola FEMSA, representing approximately 30% and 24% respectively. Consolidated operating margin decreased 0.9 percentage points from 2005 levels to 13.8% of consolidated total revenues in 2006. The decrease in operating margin was primarily attributable to the inclusion of FEMSA Cerveza's Brazilian beer operations, which generated a loss of Ps. 74 million due partly to increased marketing expenses for the brand *Kaiser* and in part to the launch of the brand *Sol*, to a margin contraction at our key beverage operations, and to the increased contribution of the Oxxo retail chain, which has the lowest operating margin relative to our other core beverage operations.

Some of our subsidiaries pay management fees to us in consideration for corporate services provided to them. These fees are recorded as administrative expenses in the respective business segments. Our subsidiaries' payments of management fees are eliminated in consolidation and, therefore, have no effect on our consolidated operating expenses.

### **Coca-Cola FEMSA**

#### *Total Revenues*

Coca-Cola FEMSA's total revenues increased 6.9% to Ps. 57,738 million in 2006 compared to Ps. 53,997 million in 2005. Net sales increased 7.3% to Ps. 57,539 million in 2006 compared to Ps. 53,601 million in 2005 and represented 99.7% of total revenues in 2006. Total revenue growth primarily resulted from Brazil, Venezuela and Mexico, accounting for approximately 34%, 18% and 17% of the incremental total revenues, respectively.

Sales volume reached 1,998 million unit cases in 2006 compared to 1,889 million unit cases in 2005, which represents an increase of 5.8%, mainly driven by a 6.4% volume growth of the *Coca-Cola* brand, which accounted for almost 70% of incremental volume. Sales volume growth in Mexico and Brazil accounted for over 57% of our incremental volume. Carbonated soft drink sales volume grew 5.9% to 1,694.7 million unit cases, driven by incremental volume across all of our territories.

Average price per unit case (calculated by dividing net sales by total sales volume excluding beer in Brazil) remained flat in real terms at Ps. 28.36 (US\$ 2.61) during 2006, due to price increases in all our territories except for Mexico and Argentina.

#### *Gross Profit*

Cost of sales increased 9.7% to Ps. 30,196 million in 2006 compared to Ps. 27,522 million in 2005. As a percentage of total sales, cost of sales increased 1.3 percentage points from 2005 to reach 52.3% of total revenues

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in 2006. The increase was mainly due to higher sweetener costs in all of our operations, combined with higher plastic bottle prices in some of our territories and higher packaging costs due to a packaging mix shift towards non-returnable presentations.

Gross profit increased 4.0% to Ps. 27,542 million in 2006 compared to Ps. 26,475 million in 2005, Brazil and Mexico accounted for over 45% of this growth. Gross margin decreased 1.3 percentage points due to higher cost per unit case in all of our territories, except Mexico and Argentina.

### *Income from Operations*

Operating expenses increased 4.8% to Ps. 18,086 million in 2006 compared to Ps. 17,257 million in 2005 mainly as a result of salary increases ahead of inflation in some of the countries in which we operate, higher operating expenses due to increases in maintenance expenses and freight costs in some territories, and higher marketing investment in our major operations in connection with several initiatives intended to reinforce our presence in the market and to build brand equity. As a percentage of total revenues, operating expenses declined from 32.0% in 2005 to 31.3% in 2006 due to higher fixed-cost absorption, driven by incremental volumes and higher average price per unit case. Administrative expenses increased 5.8% to Ps. 3,201 million in 2006 from Ps. 3,026 million in 2005. Selling expenses increased 4.6% to Ps. 14,885 million in 2006 compared to Ps. 14,231 million in 2005. At 25.8% of total revenues, selling expenses decreased 0.5 percentage points from 2005 levels.

After conducting a thorough analysis, performed by a third party, of the current conditions and expected useful life of our cooler inventories in our territories in Mexico, we decided to modify the useful life of Coca-Cola FEMSA's coolers in Mexico from five to seven years. We made this decision based on Coca-Cola FEMSA's equipment maintenance policy and our ability to better manage our cooler platform in the marketplace. This change in estimate, which was accounted for prospectively reduced our amortization expenses by Ps. 127 million in 2006, and increased our operating income by a similar amount.

Income from operations increased 2.6% to Ps. 9,456 million in 2006 compared to Ps. 9,218 million in 2005 as a result of higher fixed-cost absorption due to higher revenues. Growth in operating income in Colombia, Central America and Brazil more than compensated for flat operating income in Mexico and a decline in Venezuela and Argentina. Operating margin decreased by 0.7 percentage points to 16.4% in 2006 compared to 17.1% in 2005, mainly due to higher cost per unit case.

## **FEMSA Cerveza**

### *Total Revenues*

FEMSA Cerveza total revenues increased 24.1% to Ps. 35,599 million in 2006 as compared to Ps. 28,690 million in 2005. Net sales, which include beer and packaging sales, represented 99.4% of total revenues. This growth was primarily due to the inclusion of FEMSA Cerveza's Brazilian operations, which represented approximately 62% of the increase in total revenues. The remaining growth came from a 9.6% increase in export beer sales, a 9.3% increase in Mexican beer sales and a 6.5% increase in packaging sales.

### *Mexico*

Mexico sales volume increased 5.6% to 25.951 million hectoliters in 2006 compared to 24.580 million hectoliters in 2005. The increased product innovation, broader availability of our beers, successful execution at the point of sale, revenue management initiatives and continued strength in consumer demand, produced this top-line growth. Most notable was the growth of our *Tecate Light* and *Sol* brands, which through focused initiatives have shown improved brand equity and health indicators.

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Mexico price per hectoliter increased 3.6% to Ps. 974.4 in 2006 compared to Ps. 940.8 in 2005. This strength was driven by (1) the higher price realized from volume brought under direct distribution earlier in the year, (2) a positive mix effect and (3) revenue management and other initiatives aimed at optimizing price points per stock keeping unit and channel while selectively adjusting the margin offered to the retailer.

### Brazil

Brazil sales volume was 8.935 million hectoliters in 2006. Brazil price per hectoliter was Ps. 476.6 in 2006.

### Export

Export sales volume increased 15.3% to 2.811 million hectoliters in 2006 compared to 2.438 million hectoliters in 2005. This result was slightly above our expectations, in part due to the contribution of Heineken USA, which enabled us to outpace import category growth in the United States for a second year in a row.

Export price per hectoliter decreased 5.0% to Ps. 1,020.6 in 2006 compared to Ps. 1,074.1 in 2005. The decrease in export price reflects a negative foreign exchange rate effect due to the year-on-year real strengthening of the Mexican peso, and to a lesser extent due to presentation and channel mix effects as FEMSA Cerveza's 24-ounce presentation of *Tecate* continued to grow in the off-premise trade.

### *Gross Profit*

Cost of sales increased 32.1% to Ps. 15,271 million in 2006 compared to Ps. 11,564 million in 2005. As a percentage of total revenues, cost of sales increased 2.6 percentage points from 2005. The increase relative to total revenues growth resulted from the inclusion of our Brazilian beer operations, which has a lower gross margin compared to Mexico and exports. Excluding our Brazilian beer operations, as a percentage of revenues, cost of sales would have decreased 0.5 percentage points from 2005.

Gross profit reached Ps. 20,328 million in 2006 compared to Ps. 17,126 million in 2005, resulting in a gross margin of 57.1% as compared to 59.7%. The 2.6 percentage points decline from 2005 resulted from the inclusion of our Brazilian beer operations. Excluding our Brazilian beer operations, the gross margin would have improved 0.5 percentage points from 2005 due to the benefits of volume-driven fixed cost absorption and increased efficiency, which compensated for upward pricing pressure from raw materials, particularly aluminum.

### *Income from Operations*

Operating expenses increased 24.9% to Ps. 14,413 million in 2006 compared to Ps. 11,536 million in 2005. Administrative expenses increased 14.1% to Ps. 4,091 million in 2006 compared to Ps. 3,585 million in 2005, of which 28% of the increase corresponds to the inclusion of our Brazilian beer operations and the remaining 72% reflects changes in the distribution network, enhancements to our infrastructure and compliance-related activities. Selling expenses increased 29.8% to Ps. 10,322 million in 2006 as compared with Ps. 7,951 million in 2005. Approximately 58% of the increase in selling expenses resulted from the inclusion of the Brazilian beer operations, with most of the remaining increase (approximately 30%) resulting from increased selling expenses in the Mexican market due to the expense structure of third-party volume brought into direct distribution in the year, incremental services provided to retailers whose margins we adjust, increased activation at the point of sale and a strengthened commercial sales structure.

Income from operations increased 5.8% to Ps. 5,915 million in 2006 compared to Ps. 5,590 million in 2005. This reflects an increase in total revenues on strong volume growth and pricing, combined with higher cost of sales and operating expenses. The inclusion of Brazil resulted in a reduction of Ps. 74 million in total income from operations.

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### **FEMSA Comercio**

#### *Total Revenues*

FEMSA Comercio total revenues increased 18.7% to Ps. 35,500 million in 2006 compared to Ps. 29,898 million in 2005. The increase in total revenues was mainly a result of the aggressive expansion of the Oxxo convenience store chain, which added 706 net new Oxxo stores during 2006. As of December 31, 2006, we had 4,847 Oxxo stores nationwide. This is Oxxo's 11th consecutive year of increasing the number of net new store openings.

Same-store sales of Oxxo increased an average of 8.2% in 2006, reflecting an increase in the average customer ticket of 2.8% and an increase in store traffic of 5.4%. This increase reflects rapid store expansion and stronger category management practices, such as tailored product offerings within the stores.

#### *Gross Profit*

Cost of sales increased 17.7% to Ps. 25,866 million in 2006, below total revenue growth, compared with Ps. 21,967 million in 2005. As a result, gross profit reached Ps. 9,634 million in 2006, which represented a 21.5% increase from 2005. Gross margin expanded 0.6 percentage points to reach 27.1% of total revenues, primarily due to the benefit from increased coordinated efforts with our suppliers to provide what we believe to be the right promotions and right products for consumers.

#### *Income from Operations*

Operating expenses increased 21.3% to Ps. 8,030 million in 2006 compared with Ps. 6,621 million in 2005. Administrative expenses increased 19.4% to Ps. 727 million in 2006 compared with Ps. 609 million in 2005, due to compliance-related expenses and administrative personnel to support the expanded store base. Selling expenses increased 21.5% to Ps. 7,303 million in 2006 compared with Ps. 6,012 million in 2005, due to an increase in expenses related to the development of direct distribution capabilities, opening of new administrative offices in Colima, Tapachula and Tuxtla, an increase in energy tariffs and consumption as we continue to add to our fast-food capabilities, and increased depreciation expense due to the ongoing renovation of certain Oxxo store formats.

Income from operations increased 22.4% to Ps. 1,604 million in 2006 compared with Ps. 1,310 million in 2005. This increase was above revenue growth, and contributed to a 0.1 percentage point increase in operating margin which reached 4.5% in 2006 compared with 4.4% in 2005.

### **FEMSA Consolidated Net Income**

#### *Integral Cost of Financing*

Net interest expense reached Ps. 3,333 million in 2006 compared with Ps. 3,836 million in 2005, resulting from a lower average interest rate of 8.8% in 2006 compared to 9.3% in 2005, and a reduction in peso denominated debt, which has a higher interest rate relative to dollar denominated debt.

Foreign exchange (loss/gain) amounted to a loss of Ps. 217 million in 2006 compared with a gain of Ps. 308 million in 2005. This loss resulted from the negative effect of the weakening of the Mexican peso on our U.S. dollar-denominated debt during 2006.



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Monetary position amounted to a gain of Ps. 1,395 million in 2006 compared with a gain of Ps. 1,169 million in 2005. The increase in the amount of our gain in 2006 compared with 2005 reflects the inflation on our increased liabilities recorded in 2006.

### *Taxes*

Tax recognized in 2006, which includes income tax, tax on assets and employee profit sharing, amounted to Ps. 4,806 million compared to Ps. 4,866 million in 2005. The 1.2% decrease from 2005 is primarily due a reduction in corporate tax rates. Consequently, the effective tax rate (calculated as income before taxes and employee profit sharing divided by taxes and employee profit sharing) in 2006 was 34.3% compared to 36.2% in 2005.

### *Net Income*

Net income increased 7.3% to Ps. 9,195 million in 2006 compared to Ps. 8,566 million in 2005. This increase was due to growth of 6.0% in income from operations combined with a 13.1% decrease in net interest expense, higher gains on monetary position of 19.3%, and a reduction in the effective tax rate, partially offset by an increase in other expenses.

Net majority income amounted to Ps. 6,622 million in 2006 compared with Ps. 5,766 million in 2005, an increase of 14.8% from 2005 levels. Net majority income per FEMSA Unit (consisting of FEMSA BD Units and FEMSA B Units) was Ps. 5.552 in 2006. Net majority income per FEMSA ADS, considering an exchange rate of Ps. 10.876 per dollar, was US\$ 5.105 in 2006.

## **Results of Operations For Year Ended December 31, 2005 Compared to Year Ended December 31, 2004**

### **FEMSA Consolidated**

#### *Total Revenues*

Consolidated total revenues increased 9.1% to Ps. 111,636 million in 2005 compared to Ps. 102,316 million in 2004. Consolidated net sales increased 9.3% to Ps. 111,051 million in 2005 compared to Ps. 101,637 million in 2004. All of FEMSA's operations—soft drinks, beer, and retail—contributed positively to this high single-digit pace. FEMSA Comercio was the largest contributor to consolidated total revenue growth in 2005, representing approximately 60% of the increase. FEMSA Comercio's total revenues increased 21.8% to Ps. 29,898 million, due in large part to the 675 net new stores opened during the year. Most of the remaining growth came from Coca-Cola FEMSA and FEMSA Cerveza. Coca-Cola FEMSA's total revenues increased 5.3% to Ps. 53,997 million, mainly due to increased prices and volume growth in Mexico, Brazil and Colombia. FEMSA Cerveza posted total revenue growth of 6.9% to Ps. 28,690 million, due primarily to a 5.2% increase in total sales volume and a 2.3% increase in the total real price per hectoliter.

#### *Gross Profit*

Consolidated cost of sales increased 9.8% to Ps. 59,483 million in 2005 compared to Ps. 54,190 million in 2004. Approximately 74% of this increase resulted from FEMSA Comercio and its rapid pace of store expansion.

Consolidated gross profit increased 8.4% to Ps. 52,153 million in 2005 compared to Ps. 48,126 million in 2004, with Coca-Cola FEMSA, FEMSA Cerveza and FEMSA Comercio each representing approximately one-third of the increase. Gross margin decreased 0.3 percentage points to 46.7% of consolidated total revenues in 2005, compared to 47.0% of consolidated total revenues in 2004. We achieved an expanding or stable gross margin in all of our main business units and the slight decline in consolidated gross margin from 2004 levels resulted from the increased contribution of FEMSA Comercio in our consolidated financial results, which has a lower gross margin relative to our other operations.

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### *Income from Operations*

Consolidated operating expenses increased 7.8% to Ps. 35,750 million in 2005 compared to Ps. 33,162 million in 2004. Approximately 42% of this increase was due to FEMSA Comercio's rapid growth and 39% was attributable to FEMSA Cerveza, which increased selling expenses in connection with its new agreement with Heineken USA and also increased advertising for new products and presentations in the domestic market. As a percentage of total revenues, consolidated operating expenses declined 0.4 percentage points to reach 32.0% in 2005 compared with 32.4% in 2004.

Consolidated administrative expenses increased 3.1% to Ps. 7,466 million in 2005 versus Ps. 7,245 million in 2004. The lower level of administrative expenses relative to total revenue growth resulted from a 0.2% reduction in expenses at Coca-Cola FEMSA and a decrease in expenses as a percentage of total revenues at FEMSA Cerveza and FEMSA Comercio. As a percentage of total revenues, consolidated administrative expenses decreased 0.4 percentage points to reach 6.7% in 2005 compared with 7.1% in 2004.

Consolidated selling expenses increased 9.1% to Ps. 28,284 million in 2005 as compared to Ps. 25,917 million in 2004. Approximately 45% of this increase was due to FEMSA Comercio's rapid rate of growth, and approximately 31% was due to FEMSA Cerveza's increased expenses related to the new agreement with Heineken USA and increased advertising for new products and presentations in the domestic market. As a percentage of total revenues, selling expenses remained stable at 25.3% in 2005 compared with 25.3% in 2004.

We incur various expenses related to the distribution of our products that are accounted for in our selling expenses. During 2005 and 2004, our distribution costs amounted to Ps. 8,586 million and Ps. 7,807 million, respectively. The exclusion of these charges from our cost of sales may result in the amounts reported as gross profit not being comparable to other companies that may include all expenses related to their distribution network in cost of sales when calculating gross profit or an equivalent measure.

Consolidated income from operations increased 9.6% to Ps. 16,403 million in 2005 as compared to Ps. 14,964 million in 2004. Almost half of this increase resulted from Coca-Cola FEMSA and its solid top-line growth combined with reduced expenses. The remaining amount is attributable to FEMSA Cerveza and FEMSA Comercio, representing 34% and 23%, respectively. Consolidated operating margin increased 0.1 percentage points from 2004 levels to 14.7% of consolidated total revenues in 2005. The stable operating margin was primarily due to operating margin improvements at Coca-Cola FEMSA and FEMSA Cerveza that completely offset the increased contribution of FEMSA Comercio, which is our fastest growing business with the lowest operating margin relative to our other core operations.

Some of our subsidiaries pay management fees to FEMSA in consideration for corporate services provided to them. These fees are recorded as administrative expenses in the respective business segments. Our subsidiaries' payments of management fees are eliminated in consolidation and, therefore, have no effect on our consolidated operating expenses.

### **Coca-Cola FEMSA**

#### *Total Revenues*

Coca-Cola FEMSA's total revenues increased 5.3% to Ps. 53,997 million in 2005 compared to Ps. 51,276 million in 2004. Net sales increased 5.3% to Ps. 53,601 million in 2005 compared to Ps. 50,899 million in 2004 and represented 99.3% of total revenues in 2005. Total revenue growth primarily resulted from Mexico, Brazil and Colombia, accounting for approximately 55%, 29% and 16%, of the incremental total revenues, respectively.

Sales volume reached 1,889 million unit cases in 2005 compared to 1,812 million unit cases in 2004, which represents an increase of 4.3%. Most of the increase came from carbonated soft drink volume growth of 3.6% in 2005. The Coca-Cola brand accounted for over 50% of the incremental volume.

Average price per unit case (calculated by dividing net sales by total sales volume) increased 0.8% from Ps. 28.14 in 2004 to Ps. 28.37 in 2005. The increase was primarily due to price increases in all our territories except for Central America. Price increases implemented during the year mainly in Venezuela, Colombia and

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Argentina, combined with better packaging and product mix in Mexico and Brazil, resulted in higher average prices per unit case.

### *Gross Profit*

Cost of sales increased 4.9% to Ps. 27,522 million in 2005 compared to Ps. 26,227 million in 2004. As a percentage of total revenues, cost of sales decreased 0.2 percentage points to reach 51.0% of sales in 2005, slightly below 2004 levels. Lower sweetener costs in Mexico and Colombia, combined with the appreciation of local currencies in the majority of our territories applied to U.S. dollar-denominated costs, more than compensated for increases in prices for resin used to produce plastic bottles.

Gross profit increased 5.7% to Ps. 26,475 million in 2005 compared to Ps. 25,049 million in 2004, resulting in a gross margin of 49.0%. Brazil and Mexico accounted for 90% of this growth. Gross margin improved 0.2 percentage points as a result of higher average prices per unit case in all our territories, except for Central America, and relatively stable average costs per unit case on a consolidated basis.

### *Income from Operations*

Operating expenses increased 4.0% to Ps. 17,257 million in 2005 compared to Ps. 16,590 million in 2004. As a percentage of total revenues, operating expenses declined from 32.3% in 2004 to 32.0% in 2005 due to higher fixed-cost absorption driven by incremental volumes and higher average price per unit case. Administrative expenses declined 0.2% to Ps. 3,026 million in 2005 from Ps. 3,033 million in 2004. Selling expenses increased 5.0% to Ps. 14,231 million in 2005 compared to Ps. 13,557 million in 2004. At 26.3% of total revenues, selling expenses decreased 0.1 percentage points from 2004 levels.

Income from operations increased 9.0% to Ps. 9,218 million in 2005 compared to Ps. 8,459 million in 2004. Growth in Mexico, Brazil and Colombia more than compensated for operating income decline in Central America and Venezuela. Operating margin improved by 0.6 percentage points to 17.1% in 2005 compared to 16.5% in 2004.

## **FEMSA Cerveza**

### *Total Revenues*

FEMSA Cerveza total revenues increased 6.9% to Ps. 28,690 million in 2005 as compared to Ps. 26,848 million in 2004. Net sales increased 7.2% to Ps. 28,521 million in 2005 compared to Ps. 26,612 million in 2004. Net sales, which include beer and packaging sales, represented 99.4% of total revenues. This growth was primarily due to total beer sales volume growth of 5.2%, a 2.3% increase in total real price per hectoliter and a 2.9% increase in packaging sales.

Mexican beer sales volume increased 4.9% to 24.580 million hectoliters in 2005 compared to 23.442 million hectoliters in 2004. The increased product innovation, broader availability of our beers supported by the expansion of Oxxo, successful execution at the point of sale, and revenue management initiatives produced this top-line growth. During the year, we rolled out an unprecedented amount of new products and presentations, launching 200 new SKUs throughout the country.

Export beer sales volume increased 8.8% to 2.438 million hectoliters in 2005 compared to 2.240 million hectoliters in 2004. This result was slightly above our expectations thanks to the work of Heineken USA, which enabled us to outpace import category growth in the United States. It has been one full year since Heineken USA became our U.S. importer, and we believe that the continued focus towards increasing the overall availability of our brands and improving our performance across the entire country will continue to be important for 2006.

### *Gross Profit*

Cost of sales increased 4.7% in 2005 and as a percentage of total revenues decreased 0.9 percentage points from 2004. Cost of sales reached Ps. 11,564 million in 2005 compared to Ps. 11,048 million in 2004. Gross profit reached Ps. 17,126 million in 2005 compared to Ps. 15,800 million in 2004, resulting in a gross margin of 59.7%

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as compared to 58.8%. The gross margin expanded 0.9% as a result of higher prices per hectoliter in exports due to the new Heineken agreement structure, which did not apply in 2004, the strength of the Mexican peso as applied to U.S. dollar-denominated raw materials, and operating efficiencies.

Until January 1, 2005, we were a party to an agreement with Labatt USA for the sale of our beer in the U.S. market. Under this agreement, we sold our beer to Labatt USA at a price that gave Labatt USA margin sufficient to cover most of the selling and marketing expenses for our brands in the U.S. market and, as 30% owners of Labatt USA, we received an equivalent proportion of Labatt USA's profits as equity income. Beginning on January 1, 2005, our exports to the U.S. market are through a new commercial agreement with Heineken USA. Under this new agreement, we export our beer to the U.S. market at a higher price than under our previous arrangement with Labatt USA, and we pay a significant component of the selling and marketing expenses of our brands in the U.S. market. We no longer have any equity participation in connection with our exports to the U.S. market.

### *Income from Operations*

Operating expenses increased 7.8% to Ps. 11,536 million in 2005 compared to Ps. 10,699 million in 2004. Administrative expenses increased 2.7% to Ps. 3,585 million in 2005 compared to Ps. 3,491 million in 2004. Selling expenses increased 10.3% to Ps. 7,951 million in 2005 as compared with Ps. 7,208 million in 2004. Most of this increase was due to additional market spending under the new agreement with Heineken USA and increased domestic advertising spending for new products and presentations.

Income from operations increased 9.6% to Ps. 5,590 million in 2005 compared to Ps. 5,101 million in 2004. This reflects an increase in total revenues and reduced cost of sales relative to revenues, which more than compensated for increased operating expenses.

## **FEMSA Comercio**

### *Total Revenues*

FEMSA Comercio total revenues increased 21.8% to Ps. 29,898 million in 2005 compared to Ps. 24,556 million in 2004. The increase in total revenues was mainly a result of the aggressive expansion of the Oxxo convenience store chain, which added 675 net new Oxxo stores during 2005. As of December 31, 2005, we had 4,141 Oxxos nationwide. This is Oxxo's 10th consecutive year of increasing the number of new store openings.

Same-store sales of Oxxo increased an average of 8.7% in 2005, reflecting an increase in the average ticket of 1.3% and an increase in store traffic of 7.2%. This increase reflects rapid store expansion and stronger category management practices, such as tailored product offerings within the stores.

### *Gross Profit*

Cost of sales increased 21.8% to Ps. 21,967 million in 2005, in-line with total revenue growth, compared with Ps. 18,037 million in 2004. As a result, gross profit reached Ps. 7,931 million in 2005, which represented a 21.7% increase from 2004. Gross margin remained in-line with 2004 levels at 26.5%.

### *Income from Operations*

Operating expenses increased 19.5% to Ps. 6,621 million in 2005 compared with Ps. 5,540 million in 2004. Administrative expenses increased 4.8% to Ps. 609 million in 2005 compared with Ps. 581 million in 2004. Selling expenses increased 21.2% to Ps. 6,012 million in 2005 compared with Ps. 4,959 million in 2004. In 2005, selling expenses represented 20.1% of total revenues, remaining in line with 2004 levels, which were 20.2%.

Income from operations increased 33.8% to Ps. 1,310 million in 2005 compared with Ps. 979 million in 2004. This increase was above revenue growth, and contributed to a 0.4 percentage point increase in operating margin which reached 4.4% in 2005 compared with 4.0% in 2004.

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### **FEMSA Consolidated Net Income**

#### *Integral Result of Financing*

Net interest expense reached Ps. 3,836 million in 2005 compared with Ps. 3,463 million in 2004, despite the reduction in overall debt, resulting primarily from higher interest expense due to the conversion through currency swaps of U.S. dollar denominated debt into Mexican pesos.

Foreign exchange (loss/gain) amounted to a gain of Ps. 308 million in 2005 compared with a loss of Ps. 23 million in 2004. This significant gain resulted from the positive effect of the strength of the Mexican peso on our U.S. dollar-denominated debt during 2005.

Monetary position amounted to a gain of Ps. 1,169 million in 2005 compared with a gain of Ps. 2,112 million in 2004. The decrease in the amount of our gain in 2005 compared with 2004 reflects the lower inflation on our reduced liabilities recorded in 2005.

#### *Taxes*

Tax recognized in 2005, which includes income tax, tax on assets and employee profit sharing, amounted to Ps. 4,866 million compared to Ps. 2,649 million in 2004. The 83.7% increase from 2004 is primarily due to a one-time deferred tax benefit that was recognized at Coca-Cola FEMSA in the amount of Ps. 1,410 million during that year. Consequently, the effective tax rate (calculated as income before taxes and employee profit sharing divided by taxes and employee profit sharing) in 2005 was 36% compared to 21% in 2004.

#### *Net Income*

Net income decreased 15.1% to Ps. 8,566 million in 2005 compared to Ps. 10,085 million in 2004. This decrease was due to higher taxes relative to 2004 because of the one-time deferred tax benefit recognized at Coca-Cola FEMSA during 2004, to higher interest expense as we continued to convert our U.S. dollar denominated debt into Mexican pesos and to a lower monetary gain due to the lower inflationary impact on our reduced liabilities recorded in 2005.

Net majority income amounted to Ps. 5,766 million in 2005 compared with Ps. 6,411 million in 2004, a decrease of 10.1% from 2004 levels. Net majority income per FEMSA Unit was Ps. 4.834 for full year 2005. Net majority income per ADS, considering an exchange rate of Ps. 10.711 per dollar, was US\$ 4.51 in 2005.

### **Liquidity and Capital Resources**

#### **Liquidity**

Each of our sub-holding companies generally finances its operational and capital requirements on an independent basis. As of December 31, 2006, 89.5% of our outstanding consolidated indebtedness was at the level of our sub-holding companies. This structure is attributable, in part, to the inclusion of third parties in the capital structure of Coca-Cola FEMSA. Currently, we expect to continue to finance our operations and capital requirements primarily at the level of our sub-holding companies. Nonetheless, we may decide to incur indebtedness at our holding company in the future to finance the operations and capital requirements of our subsidiaries or significant acquisitions, investments or capital expenditures. As a holding company, we depend on dividends and other distributions from our subsidiaries to service our indebtedness.

We continuously evaluate opportunities to pursue acquisitions or engage in joint ventures or other transactions. We would expect to finance any significant future transactions with a combination of cash from operations, long-term indebtedness and capital stock.

The principal source of liquidity of each sub-holding company has generally been cash generated from operations. We have traditionally been able to rely on cash generated from operations because a significant majority of the sales of Coca-Cola FEMSA, FEMSA Cerveza and FEMSA Comercio are on a cash or short-term credit basis, and FEMSA Comercio's Oxxo stores are able to finance a significant portion of their initial and ongoing inventories with supplier credit. Our principal use of cash has generally been for capital expenditure

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programs, debt repayment and dividend payments. The following is a summary of the principal uses of cash for the three years ended December 31, 2006:

**Principal Uses of Cash**

	<b>For the Year Ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
	<b>(in millions of constant Mexican pesos)</b>		
Net resources generated by operations	Ps. 16,139	Ps. 14,337	Ps. 16,654
Capital expenditures <sup>(1)</sup>	(8,888)	(7,034)	(7,508)
Bank loans and notes	4,527	(12,027)	7,229
Dividends declared and paid	(1,406)	(1,063)	(907)

(1) Includes property, plant and equipment plus intangible assets and other assets.

Our sub-holding companies generally incur short-term indebtedness in the event that they are temporarily unable to finance operations or meet any capital requirements with cash from operations. A significant decline in the business of any of our sub-holding companies may affect the sub-holding company's ability to fund its capital requirements. A significant and prolonged deterioration in the economies in which we operate or in our businesses may affect our ability to obtain short-term and long-term credit or to refinance existing indebtedness on terms satisfactory to us.

We have traditionally financed significant acquisitions, principally Coca-Cola FEMSA's acquisition of Coca-Cola Buenos Aires in 1994 and its acquisition of Panamco in May 2003 and our acquisition of the 30% interest in FEMSA Cerveza owned by affiliates of InBev in August 2004, capital expenditures and other capital requirements that could not be financed with cash from operations by incurring long-term indebtedness and through the issuance of equity.

Our consolidated total indebtedness was Ps. 40,181 million as of December 31, 2006, as compared to Ps. 36,105 million as of December 31, 2005. Short-term debt (including maturities of long-term debt) and long-term debt were Ps. 5,930 million and Ps. 34,251 million, respectively, as of December 31, 2006, as compared to Ps. 5,163 million and Ps. 30,942 million, respectively, as of December 31, 2005. Cash and cash equivalents were Ps. 7,936 million as of December 31, 2006, as compared to Ps. 8,558 million as of December 31, 2005.

We believe that our sources of liquidity as of December 31, 2006 were adequate for the conduct of our sub-holding companies' businesses and that we will have sufficient funds available to meet our expenditure demands and financing needs in 2007.

**Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements.

**Table of Contents****Contractual Obligations**

The table below sets forth our contractual obligations as of December 31, 2006:

	Less than 1 year	1 - 3 years	Maturity 3 - 5 years	In excess of 5 years	Total
(in millions of Mexican pesos)					
<b>Long-Term Debt</b>					
Mexican pesos <sup>(1)</sup>	Ps. 2,082	Ps. 7,286	Ps. 8,909	Ps. 11,486	Ps. 29,763
U.S. dollars <sup>(1)</sup>	147	3,821	132	2,435	6,535
Colombian pesos	166				166
Brazilian reais	38	180			218
<b>Capital Leases</b>					
U.S. dollars	7	2			9
<b>Interest payments<sup>(2)</sup></b>					
Mexican pesos	2,429	4,100	2,894	2,003	11,426
U.S. dollars	421	798	289	173	1,681
Colombian pesos	16				16
Brazilian reais	15	11			26
<b>Interest rate swaps<sup>(3)</sup></b>					
Mexican pesos	341	(1,506)	(781)	(107)	(2,053)
U.S. dollars					
<b>Cross currency and interest rate swap</b>					
Japanese yen to Brazilian reais <sup>(4)</sup>	12	41			53
Mexican pesos to U.S. dollars <sup>(5)</sup>		(4)	(13)		(17)
U.S. dollars to Colombian pesos <sup>(6)</sup>		64			64
<b>Forward contracts</b>					
Agreements to purchase Mexican pesos <sup>(7)</sup>	(41)				(41)
Agreements to purchase euros	(2)				(2)
<b>Operating leases</b>					
Mexican pesos	1,037	2,072	1,956	6,470	11,535
U.S. dollars	508	291	46		845
Colombian pesos	5	3			8
Brazilian reais	62	130	87		279
Argentine pesos	4				4
<b>Commodity price contracts</b>					
U.S. dollars	895	134			1,029
<b>Purchase obligations</b>					
	192	556			748
<b>Expected benefits to be paid for pension plans, seniority premiums, post-retirement medical benefits and severance indemnities</b>					
	534	827	821	2,000	4,182
<b>Other long-term liabilities<sup>(8)</sup></b>					
				4,625	4,625

(1) Includes the effect of a cross currency swap, pursuant to which ¥1,639 million of denominated in Japanese yen long-term debt is swapped for Brazilian reais, in the amount of Ps. 151 million.

(2) Interest was calculated using long-term debt as of and interest rate amounts in effect on December 31, 2006. The debt and applicable interest rates in effect are shown in note 19 to our audited consolidated financial statements. Liabilities denominated in U.S. dollars were translated to Mexican pesos at an exchange rate of Ps. 10.8755 per U.S. dollar, the exchange rate quoted to us by dealers for the settlement of obligations in foreign currencies on December 31, 2006.

- (3) Reflects the amount of future payments that we would be required to make. The amounts were calculated by applying the difference between the interest rate swaps and the nominal interest rates contracted to long-term debt as of December 31, 2006.



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- (4) Includes (1) the cross currency swap from Japanese yen to Brazilian reais with respect to ¥4,267 million of Japanese yen-denominated debt using the contracted exchange rate of .018304 per Brazilian reais, (2) the interest rate swap from a fixed Japanese yen interest rate to a variable Brazilian reais interest rate, which have averages of 5.7% and 14.0%, respectively.
- (5) Includes cross-currency swaps from Mexican pesos to U.S. dollars with a notional amount of Ps.1, 091 million with maturity dates of September 15, 2008 and Ps. 1,317 million with a settlement date of December 5, 2011.
- (6) Includes cross-currency swaps from U.S. dollars to Colombian pesos with a notional amount of US\$40 million with a maturity date of September 10, 2008.
- (7) Forward contract with respect to Ps. 922 million with a settlement date of June 29, 2007, and Ps. 222 million with a settlement date of August 30, 2007, paying U.S. dollars and receiving Mexican pesos held as of December 31, 2006.
- (8) Other long-term liabilities includes principally contingencies and derivative financial instruments. Other long-term liabilities additionally reflects those liabilities whose maturity date is undefined and depends on a series of circumstances out of our control, therefore these liabilities have been considered to have a maturity of more than five years.  
As of December 31, 2006, Ps. 5,930 million of our total consolidated indebtedness was short-term debt (including maturities of long-term debt).

As of December 31, 2006, our consolidated average cost of borrowing, after giving effect to the cross currency and interest rate swaps, was approximately 8.8%, compared to 9.3% in 2005. The decrease in our average cost of borrowing mainly reflects a decrease in the London interbank offered rate, or LIBOR, the *Tasa de Interés Interbancaria de Equilibrio* (Equilibrium Interbank Interest Rate), or TIEE, and the *Certificados de la Tesorería* (Treasury Certificates), or CETES, rate. As of December 31, 2006, after giving effect to cross currency swaps, 20.7% of our total consolidated indebtedness was denominated and payable in U.S. dollars, 75.1% was in Mexican pesos, 1.4% was in Brazilian reais, 1.1% was in Venezuelan bolivars, 1.3% was in Argentine pesos and the remaining 0.4% was in Colombian pesos.

**Table of Contents****Overview of Debt Instruments**

The following table shows the allocations of total debt of our company as of December 31, 2006:

	Total Debt Profile of the Company				Total Debt
	FEMSA and others <sup>(1)</sup>	Coca-Cola FEMSA	FEMSA Cerveza	FEMSA Comercio	
(in millions of constant Mexican pesos)					
<b>Short-term Debt</b>					
<i>U.S. dollars:</i>					
Bank loans		Ps. 141	Ps. 1,650		Ps. 1,791
<i>Mexican pesos:</i>					
Bank loans			406		406
<i>Brazilian reais:<sup>(2)</sup></i>					
Bank loans			344		344
<i>Venezuelan bolivars:</i>					
Bank loans		422			422
<i>Argentine pesos:</i>					
Bank loans		527			527
<b>Long-term Debt<sup>(3)</sup></b>					
<i>U.S. dollars:</i>					
Bank loans		2,447	855		3,302
Yankee bond		3,233			3,233
Leasing		9			9
<i>Mexican pesos:</i>					
Bank loans	1,712	5,250	13,145		20,107
Notes	2,500	7,156			9,656
<i>Colombian pesos:</i>					
Notes		166			166
<i>Brazilian reais:<sup>(2)</sup></i>					
Bank Loans			218		218
<b>Total</b>	Ps. 4,212	Ps. 19,351	Ps. 16,618		Ps. 40,181
<b>Average Cost<sup>(4)</sup></b>					
U.S. dollars		6.6%	5.8%		6.3%
Mexican pesos	9.9%	9.1%	9.3%		9.3%
Colombian pesos		9.3%			9.3%
Venezuelan bolivars		9.6%			9.6%
Argentine pesos		10.6%			10.6%
Brazilian reais			13.4%		13.4%
<b>TOTAL</b>	9.9%	8.4%	8.9%		8.8%

(1) Ps. 2,500 million of *certificados bursátiles* of FEMSA are guaranteed by FEMSA Cerveza and a Ps. 1,712 million bank loan of FEMSA is guaranteed by FEMSA Comercio.

(2) Includes the effect of cross currency swaps in the amount of Ps. 393 million from Japanese yen to Brazilian reais.

(3) Includes the Ps. 2,440 million current portion of long-term debt.

(4) Includes the effect of cross currency and interest rate swaps.

**Restrictions Imposed by Debt Instruments**

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Generally, the covenants contained in the credit agreements and other instruments governing indebtedness entered into by us or our sub-holding companies include limitations on the incurrence of any additional debt based on debt service coverage ratios or leverage tests. These credit agreements also generally include restrictive covenants applicable to us, our sub-holding companies and their subsidiaries. There are no cross-guarantees between sub-holding companies, and we have not provided guarantees with respect to any of the debt obligations

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of our sub-holding companies. FEMSA Cerveza has guaranteed FEMSA's obligation under its *certificados bursátiles*. Certain of our financing instruments mentioned above are subject to either acceleration or repurchase at the lender's or holder's option if, in the case of FEMSA, the persons exercising control over FEMSA no longer exercise such control and, in the case of FEMSA Cerveza, FEMSA ceases to control FEMSA Cerveza.

We are in compliance with all of our restrictive covenants as of December 31, 2006. A significant and prolonged deterioration in our consolidated results of operations could cause us to cease to be in compliance under certain indebtedness in the future. We can provide no assurances that we will be able to incur indebtedness or to refinance existing indebtedness on similar terms in the future.

### **Summary of Debt**

The following is a summary of our indebtedness by sub-holding company and for FEMSA as of December 31, 2006:

*Coca-Cola FEMSA.* Coca-Cola FEMSA's total indebtedness was Ps. 19,351 million as of December 31, 2006, as compared to Ps. 21,005 million as of December 31, 2005. Short-term debt and long-term debt were Ps. 3,170 million and Ps. 16,181 million, respectively, as of December 31, 2006, as compared to Ps. 4,690 million and Ps. 16,315 million, respectively, as of December 31, 2005. Cash and cash equivalents comprised mainly of Mexican pesos, Brazilian reais and U.S. Dollars, representing 37%, 26% and 22%, respectively. As of December 31, 2006, cash and cash equivalents were Ps. 4,473, as compared to Ps. 2,122 million as of December 31, 2005. Approximately Ps. 250 million of cash is considered restricted cash because it has been deposited to settle accounts payable in Venezuela and in Brazil.

As part of our financing policy, we expect to continue to finance our liquidity needs from cash operations. Nonetheless, as a result of regulations in certain countries in which we operate, it may not be beneficial or, as the case of exchange controls in Venezuela, practicable for us to remit cash generated in local operations to fund cash requirements in other countries. In the event that cash from operations in these countries is not sufficient to fund future working capital requirements and capital expenditures, we may decide, or be required, to fund cash requirements in these countries through local borrowings rather than remitting funds from another country. In addition, in the future we may be required to finance our working capital and capital expenditure needs with short-term debt or other borrowings.

Coca-Cola FEMSA's average cost of debt, after giving effect to cross currency and interest rate swaps, was 7.0% in U.S. dollars, 9.5% in Mexican pesos, 8.0% in Colombian pesos, 11.3% in Venezuelan bolivars and 9.7% in Argentine pesos as of December 31, 2006 compared to 7.7% in U.S. dollars, 9.3% in Mexican pesos, 8.7% in Colombian pesos, 12.1% in Venezuelan bolivars, and 9.4% in Argentine pesos as of December 31, 2005.

*FEMSA Cerveza.* As of December 31, 2006, FEMSA Cerveza's total outstanding debt was Ps. 16,618 million, which included Ps. 2,399 million of outstanding short-term trade and working capital loans. As of December 31, 2006, FEMSA Cerveza had approximately Ps. 14,219 million of long-term debt outstanding that included Ps. 14,219 million consisting of bilateral bank loans and equipment financing loans. Cash and cash equivalents comprised of Mexican pesos, Brazilian reais and US Dollars, representing 71%, 19% and 9%, respectively. As of December 31, 2006, cash and cash equivalents were Ps. 1,862 as compared to Ps. 3,751 as of December 31, 2005. FEMSA Cerveza's average cost of debt, after giving effect to interest rate swaps, as of December 31, 2006 was 9.47% in Mexican pesos and 4.49% in U.S. dollars.

*FEMSA Comercio.* As of December 31, 2006, FEMSA Comercio does not have outstanding debt.

*FEMSA and other business segment.* As of December 31, 2006, FEMSA and the companies comprising our other business segment had total outstanding debt of Ps. 4,212 million, all of which was long term. This consisted of Ps. 2,500 million of *certificados bursátiles*, that are guaranteed by

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FEMSA Cerveza, and a Ps. 1,712 million bank loan guaranteed by FEMSA Comercio, and that mature in July 2009 and in August 2010, respectively. Additionally, as of December 31, 2006, FEMSA had Ps. 1,762 million in bank loan debt that it incurred in connection with the 30% equity acquisition of FEMSA Cerveza. The debt of the other business segment consisted of Ps. 72 million in bank loans denominated in U.S. dollars, of which Ps. 14 million matures in July 2008 and Ps. 58 million matures in September 2009. FEMSA and our other business segments had an average cost of debt, after giving effect to interest rate swaps as of December 31, 2006 of 9.35% in Mexican pesos.

**Contingencies**

We have various loss contingencies, for which reserves have been recorded in those cases where we believe the results of an unfavorable resolution is probable. See Item 8. Financial Information Legal Proceedings. Most of these loss contingencies have been recorded as reserves against intangibles recorded as a result of the Panamco acquisition. Any amounts required to be paid in connection with these loss contingencies would be required to be paid from available cash.

The following table presents the nature and amount of the loss contingencies as of December 31, 2006:

	<b>Loss Contingencies As of December 31, 2006 (in millions of constant Mexican pesos)</b>	
Tax	Ps.	1,549
Legal		219
Labor		512
<b>TOTAL</b>	<b>Ps.</b>	<b>2,280</b>

As is customary in Brazil, we have been asked by the tax authorities to collateralize tax contingencies currently in litigation amounting to Ps. 1,415 million by pledging fixed assets and entering into available lines of credit.

We have other loss contingencies for which we have not recorded a reserve. These contingencies or our assessment of them may change in the future, and we may record reserves or be required to pay amounts in respect of these contingencies.

**Capital Expenditures**

For the past five years, we have had significant capital expenditure programs, which for the most part were financed with cash from operations. Capital expenditures reached Ps. 8,888 million in 2006 compared to Ps. 7,034 million in 2005, an increase of 26.4%. This was primarily due to an increase in capital expenditures at FEMSA Cerveza and FEMSA Comercio. The principal components of our capital expenditures have been for equipment, market-related investments and production capacity and distribution network expansion at both Coca-Cola FEMSA and FEMSA Cerveza and the construction of new Oxxo stores at FEMSA Comercio. See Item 4. Information on the Company Capital Expenditures and Divestitures.

*Expected Capital Expenditures for 2007*

Our capital expenditure budget for 2007 is expected to be approximately Ps. 11,263 million. The following discussion is based on each of our sub-holding companies' internal 2007 budgets. The capital expenditure plan for 2007 is subject to change based on market and other conditions and the subsidiaries' results of operations and financial resources.

Coca-Cola FEMSA's capital expenditures in 2007 are expected to be approximately Ps. 3,688 million. Coca-Cola FEMSA's capital expenditures in 2007 are primarily intended for:

investments in returnable bottles and cases;



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market investments (primarily for the placement of refrigeration equipment); and

improvements in our manufacturing facilities and throughout our logistics network.

Coca-Cola FEMSA estimates that a majority of projected capital expenditures for 2007 will be spent in Mexican territories.

FEMSA Cerveza's capital expenditure budget for 2007 is expected to be approximately Ps. 5,278 million. FEMSA Cerveza expects to allocate part of this budget for investments in its manufacturing facilities in Mexico and Brazil, predominantly related to marginal capacity expansions of its breweries and equipment modernization. FEMSA Cerveza also expects to apply a portion of this budget towards the improvement of its distribution assets, including new and replacement vehicles, the maintenance of a secondary distribution fleet and its enterprise resource planning and information technology systems. In addition, FEMSA Cerveza plans to invest in commercial and market-related activities such as the enhancement of its retail coverage, the acquisition of third party distributors, the development of long-term sponsorships and the placement of refrigeration equipment nationwide.

FEMSA Comercio's capital expenditure budget in 2007 is expected to total approximately Ps. 1,741 million, and will be allocated to the opening of new Oxxo stores and to a lesser extent to the refurbishing of existing Oxxo stores. In addition, investments are planned in FEMSA Comercio's information technology, ERP software systems and transportation equipment.

**Hedging Activities**

Our business activities require the holding or issuing of derivative instruments to hedge our exposure to market risks related to changes in interest rates, foreign currency exchange rates, equity risk and commodity price risk. See Item 11. Quantitative and Qualitative Disclosures about Market Risk.

The following table provides a summary of the fair value of derivative instruments as of December 31, 2006. The fair market value is obtained mainly from external sources, which are our counterparties to the contracts.

	Fair Value At December 31, 2006				Total fair value
	Maturity less than 1 year	Maturity 1 - 3 years	Maturity 3 - 5 years	Maturity in excess of 5 years	
Prices quoted by external sources	(127)	(235)	(412)	(207)	(981)

**Plan for the Disposal of Certain Fixed Assets**

We have identified certain fixed assets consisting of land, buildings and equipment for disposal, and we have an approved program for disposal of these fixed assets. These assets are not in use and have been valued at their estimated realizable value, according to independent appraisals. These assets are allocated as follows:

	December 31,	
	2006	2005
	(in millions of constant Mexican pesos)	
Coca-Cola FEMSA	Ps. 166	Ps. 199
FEMSA Cerveza	283	260
FEMSA and other	296	306

Total Ps. 745 Ps. 765

Fixed assets recorded at their estimated realizable value are considered monetary assets on which a loss on monetary position is computed and recorded in results of operation.





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### **U.S. GAAP Reconciliation**

The principal differences between Mexican Financial Reporting Standards and U.S. GAAP that affect our net income and majority stockholders equity relate to the accounting treatment of the following items:

consolidation of our subsidiary Coca-Cola FEMSA, which is a consolidated subsidiary for purposes of Mexican Financial Reporting Standards but presented under the equity method for U.S. GAAP purposes;

FEMSA's minority interest acquisition;

deferred income taxes and deferred employee profit sharing;

restatement of imported machinery and equipment;

capitalization of integral result of financing; and

start-up expenses.

For a more detailed description of the differences between Mexican Financial Reporting Standards and U.S. GAAP as they relate to us, as well as U.S. GAAP consolidated balance sheets, statements of income, changes in stockholders' equity and cash flows for the same periods presented for Mexican Financial Reporting Standards purposes and a reconciliation of net income and stockholders' equity under Mexican Financial Reporting Standards to net income and stockholders' equity under U.S. GAAP, see notes 27 and 28 to our audited consolidated financial statements.

Pursuant to Mexican Financial Reporting Standards, our audited consolidated financial statements recognize certain effects of inflation in accordance with Bulletin B-10 and B-12. These effects were not reversed in our U.S. GAAP financial information.

Under U.S. GAAP, we had net income of Ps. 6,720 million and Ps. 5,840 million in 2006 and 2005, respectively. Under Mexican Financial Reporting Standards, we had net majority income of Ps. 6,622 million and Ps. 5,766 million in 2006 and 2005, respectively. In 2005, net income under U.S. GAAP was higher than net majority income under Mexican Financial Reporting Standards, mainly as a result of the effect of deferred income taxes, deferred employee profit sharing and severance indemnities.

Stockholders' equity under U.S. GAAP as of December 31, 2006 and 2005 was Ps. 71,246 million and Ps. 66,070 million, respectively. Under Mexican Financial Reporting Standards, majority stockholders' equity as of December 31, 2006 and 2005 was Ps. 54,220 million and Ps. 50,027 million, respectively. The principal reasons for the difference between stockholders' equity under U.S. GAAP and majority stockholders' equity under Mexican Financial Reporting Standards were the effect of the goodwill generated by the minority interest acquisition, the capitalization of the integral result of financing and the effect of deferred income tax, partially offset by the effects of deferred employee profit sharing and start-up expenses.

### **ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES**

#### **Directors**

Management of our business is vested in the board of directors and in our chief executive officer. Our bylaws provide that the board of directors will consist of no more than 21 directors and designated alternate directors elected by our shareholders at the annual ordinary general shareholders meeting. Directors are elected for a term of one year. Alternate directors are authorized to serve on the board of directors in place of their specific directors who are unable to attend meetings and may participate in the activities of the board of directors. Nineteen members were

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elected to serve on our board of directors for the 2007 year. Our bylaws provide that the holders of the Series B Shares elect at least 11 directors and that the holders of the Series D Shares elect five directors. The shareholders may designate alternate directors to cover the absence of a specific director. Upon the issuance of Series L Shares or upon the conversion of the Series D-L Shares, the holders of the Series L Shares will be entitled to elect two directors. See Item 10. Additional Information Bylaws.

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In accordance with our bylaws and article 24 of the Mexican Securities Law, at least 25% of the members of our board of directors must be independent.

The board of directors may designate interim directors in the case that a director is absent or an elected director and corresponding alternate are unable to serve. Such interim directors shall serve until the next shareholders meeting, at which the Shareholders shall elect a replacement.

Our bylaws provide that the board of directors shall meet at least once every 3 months. Actions by the board of directors must be approved by at least a majority of the directors present and voting. The chairman of the board of directors, the chairman of our Audit Committee or Corporate Practices Committee, or at least 25% of our directors may call a board of directors meeting and include matters in the meeting agenda.

***Series B Directors***

Eugenio Garza Lagüera Born: December 1923

*Director and Honorary Life Chairman* First elected: 1960

Term expires: 2008

Other directorships: Honorary Life Chairman of Coca-Cola FEMSA, Instituto Tecnológico de Estudios Superiores de Monterrey (ITESM) and BBVA Bancomer

Business experience: Joined FEMSA in 1946 in the research department of Cuauhtémoc

Education: Holds degrees in chemical engineering from the University of Texas and in business administration from ITESM

Alternate director: Mariana Garza de Treviño<sup>(1)(2)</sup>

José Antonio Fernández Carbajal<sup>(3)</sup> Born: February 1954

*Director and Chairman of the Board* First elected 2001

(Chairman):

First elected 1984

(Director):

Term expires: 2008

Principal occupation: Chief Executive Officer of FEMSA

Other directorships: Chairman of the board of Coca-Cola FEMSA, Vice-Chairman of the board of ITESM and member of the boards of BBVA Bancomer, Grupo Industrial Saltillo, S.A.B. de C.V., Industrias Peñoles, S.A. de C.V., Grupo Bimbo, S.A.B. de C.V., Grupo Televisa, S.A.B. and Controladora Vuela Compañía de Aviación S.A. de C.V. ( Volaris )

Business experience: Joined FEMSA s strategic planning department in 1987, held managerial positions at FEMSA Cerveza s commercial division and Oxxo and appointed our Chief Executive Officer in 1995

Education: Holds a degree in industrial engineering and an MBA from ITESM

Alternate director: Federico Reyes García

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Bárbara Garza de Braniff (1)(2)	Born:	April 1958
<i>Director</i>	First elected:	2005
	Term expires:	2008
	Principal occupation:	Private investor
	Business experience:	Former President / Chief Executive Officer of Alternativas Pacíficas, A.C., (a non-profit organization)
	Education:	Holds a business administration degree from ITESM
	Alternate director:	Eva Garza de Fernández <sup>(1)(4)</sup>
José Calderón Rojas	Born:	July 1954
<i>Director</i>	First elected:	2005
	Term expires:	2008
	Principal occupation:	Chairman of the board of Directors and Executive Vice-President of Servicios Administrativos de Monterrey, S.A. de C.V. and Franca Industrias, S.A. de C.V.
	Other directorships:	Member of the Board of BBVA Bancomer
	Education:	Holds a law degree from the Universidad Autónoma de Nuevo León (UANL) and completed specialization studies in tax at UANL
	Alternate director:	Francisco José Calderón Rojas <sup>(5)</sup>
Consuelo Garza de Garza <sup>(6)</sup>	Born:	October 1930
<i>Director</i>	First elected:	1995
	Term expires:	2008
	Business experience:	Founder and former President of Asociación Nacional Pro-Superación Personal, (a non-profit organization)
	Alternate director:	Alfonso Garza Garza <sup>(7)</sup>
Max Michel Suberville	Born:	July 1932
<i>Director</i>	First elected:	1985
	Term expires:	2008
	Principal occupation:	Honorary Chairman of the Board of El Puerto de Liverpool, S.A.B. de C.V.
	Other directorships:	Member of the boards of Grupo Lamosa, S.A.B. de C.V., Industrias Peñoles, S.A. de C.V., and Grupo Nacional Provincial, S.A.
	Education:	Holds a graduate degree from The Massachusetts Institute of Technology and completed post-graduate studies at Harvard University
	Alternate director:	Max Michel González <sup>(8)</sup>

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Alberto Bailleres <i>Director</i>	Born:	August 1931
	First elected:	1995
	Term expires:	2008
	Principal occupation:	Executive President of Industrias Peñoles, S.A. de C.V., Grupo Nacional Provincial, S.A. and Grupo BAL, S.A. de C.V.
	Other directorships:	Chairman of the Board of Industrias Peñoles, S.A. de C.V., Grupo Nacional Provincial, S.A. and Grupo Palacio de Hierro, S.A. de C.V., member of the boards of BBVA Bancomer, Grupo Televisa, S.A.B., Grupo Kuo, S.A.B. de C.V. (formerly Grupo Desc) and Valores Mexicanos Casa de Bolsa, S.A. de C.V.
	Education:	Holds an economics degree from Instituto Tecnológico Autónomo de México
Francisco Javier Fernández Carbajal <sup>(9)</sup> <i>Director</i>	Alternate director:	Arturo Fernández Pérez
	Born:	April 1955
	First elected:	2005
	Term expires:	2008
	Principal occupation:	Private business consultant
	Education:	Holds degrees in mechanical and electrical engineering from ITESM and an MBA from Harvard Business School
Ricardo Guajardo Touché <i>Director</i>	Alternate director:	Javier Astaburuaga Sanjines
	Born:	May 1948
	First elected:	1988
	Term expires:	2008
	Principal occupation:	Former Chairman of the Board of BBVA Bancomer
	Other directorships:	Member of the Board of El Puerto de Liverpool, S.A.B. de C.V., Alfa, S.A.B. de C.V., BBVA Bancomer, Grupo Aeroportuario del Sureste, S.A. de C.V. and ITESM
Alfredo Livas Cantú <i>Director</i>	Business experience:	Has held senior executive positions in our company, Grupo AXA, S.A. de C.V. and Valores de Monterrey, S.A. de C.V.
	Education:	Holds degrees in electrical engineering from ITESM and the University of Wisconsin and a masters degree from the University of California at Berkeley
	Alternate director:	Othón Páez Garza <sup>(10)</sup>
	Born:	July 1951
	First elected:	1995
	Term expires:	2008
Alfredo Livas Cantú <i>Director</i>	Principal occupation:	President of Praxis Financiera, S.C.
	Other directorships:	Member of the boards of Grupo Jomar, S.A. de C.V. and British American Tobacco (Mexican board)
	Business experience:	Joined FEMSA in 1978 and held several positions in the areas of financial planning and treasury and served as Chief Financial Officer from 1989 to 1999
	Education:	Holds an economics degree from UANL and an MBA and masters degree in economics from the University of Texas



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	Alternate Director:	Sergio Deschamps Ebergenyi
Roberto Servitje Sendra <i>Director</i>	Born:	January 1928
	First elected:	1995
	Term expires:	2008
	Principal occupation:	Chairman of the Board of Grupo Bimbo, S.A.B. de C.V.
	Other directorships:	Member of the board of DaimlerChrysler de México, S.A.
	Business experience:	Founding member and active Chairman of Grupo Bimbo, S.A.B. de C.V.
	Education:	Holds a PMD degree from Harvard University
	Alternate director:	Juan Guichard Michel <sup>(8)</sup>
Carlos Salguero <i>Director</i>	Born:	October 1929
	First elected:	1995
	Term expires:	2008
	Business experience:	Former Executive Vice President of Phillip Morris International
	Other directorships:	Former member of the boards of Tabacalera Mexicana, S.A. de C.V., Tabacalera Costarricense, S.A., Tabacalera Centroamericana, S.A. and other Latin American companies
	Education:	Holds a business degree from the Columbian Faculty of Economic Sciences, postgraduate studies in economics and management from Albany Business College and University College (Syracuse) and received an Honor for Civil Merit by H.M. the King of Spain in 1995
	Alternate director:	Alfonso González Migoya
Paulina Garza de Marroquín <sup>(1)(2)</sup> <i>Director</i>	Born:	March 1972
	First elected:	1999 as alternate; 2004 as main Board Member
	Term expires:	2008
	Business experience:	Private Investor
	Education:	Holds a business administration degree from ITESM
	Alternate director:	Carlos Salazar Lomelín
José Manuel Canal Hernando <i>Director</i>	Born:	February 1940
	First elected:	2003
	Term expires:	2008
	Principal occupation:	Private consultant
	Other directorships:	Member of the Board of Coca-Cola FEMSA and member of its audit committee; Board Member of ALSEA, S.A. de C.V. and chairman of the audit committee of Instituto del Fondo Nacional de la Vivienda para los Trabajadores (INFONAVIT)
	Business experience:	Former managing partner at Ruiz, Urquiza y Cía, S.C. from 1981 to 1999, acted as our statutory examiner from 1984 to 2002, presided in the Committee of Surveillance of the Mexican Institute of Finance Executives, has participated in several commissions at the Mexican Institute of Public Accountants and has extensive experience in financial auditing for holding companies, banks and financial brokers
	Education:	Holds a CPA degree from the Universidad Nacional Autónoma de México
	Alternate director:	Ricardo Saldívar Escajadillo

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***Series D***

***Directors***

<p>Armando Garza Sada <i>Director</i></p>	<p>Born: June 1957                      First elected: 2006                      Term expires: 2008                      Principal occupation: Executive Vice-President of Corporate Development of Alfa, S.A.B. de C.V.                      Other directorships: Member of the Board of Directors of Alfa, S.A.B. de C.V., Grupo Gigante, S.A. de C.V. and Grupo MVS, S.A. de C.V., El Puerto de Liverpool. S.A.B. de C.V., Grupo Lamosa S.A.B. de C.V. and ITESM                      Business experience: He has a long professional career in Alfa, S.A.B. de C.V., former Chief Executive Officer at Sigma Alimentos, S.A. de C.V.                      Education: Holds a degree in industrial engineering from ITESM and a MBA from Stanford University                      Alternate director: Eduardo Padilla Silva</p>
<p>Alexis E. Rovzar de la Torre <i>Director</i></p>	<p>Born: July 1951                      First elected: 1989                      Term expires: 2008                      Principal occupation: Executive Partner at White &amp; Case, S.C. law firm                      Other directorships: Member of the boards of Coca-Cola FEMSA (chairman of its audit committee), Grupo Bimbo, S.A.B. de C.V., Deutsche Bank (Mexico), Grupo ACIR, S.A. de C.V. and COMEX, S.A. de C.V.                      Business experience: Expert in private and public mergers and acquisitions as well as other aspects of financial law and has been advisor to many companies on international business and joint venture transactions                      Education: Holds a law degree from the Universidad Nacional Autónoma de México                      Alternate director: Francisco Zambrano Rodríguez</p>
<p>Helmut Paul <i>Director</i></p>	<p>Born: March 1940                      First elected: 1988                      Term expires: 2008                      Principal occupation: Owner of H. Paul &amp; Company LLC (a corporate finance advisory firm)                      Other directorships: Member of the Board of Zurich Emerging Markets Solutions                      Business experience: Has held several managing positions in the International Finance Corporation, mainly responsible for Latin American and Caribbean investments                      Education: Holds an MBA from the University of Hamburg                      Alternate director: Antonio Elosúa Mugerza</p>



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Lorenzo H. Zambrano <i>Director</i>	Born: First elected: Term expires: Principal occupation: Other directorships:  Education:  Alternate director:	March 1944 1995 2008 Chairman and Chief Executive Officer of Cemex, S.A.B. de C.V. Member of the boards of IBM Corporation, Alfa, S.A.B. de C.V. (Human Resources Committee), Vitro, S.A.B. de C.V. (Chairman of the Compensation Committee), Grupo Televisa, S.A.B. and Grupo Financiero Banamex, S.A. de C.V., and member of Citigroup's International Advisory Board.  Holds a degree in mechanical engineering and administration from ITESM and an MBA from Stanford University Francisco Garza Zambrano
Robert E. Denham <i>Director</i>	Born: First elected: Term expires: Principal occupation: Other directorships:  Business experience:  Education:  Alternate director:	August 1945 2001 2008 Partner of Munger, Tolles & Olson LLP law firm Member of the Boards of Wesco Financial Corporation, US Trust Company, Lucent Technologies, Inc. and Chevron Corp.  Former Chief Executive Officer of Salomon Inc., representative to the APEC Business Advisory Council and member of the OECD Business Sector Advisory Group on Corporate Governance  <i>Magna cum laude</i> graduate from the University of Texas, holds a JD from Harvard Law School and a masters degree in Government from Harvard University José González Ornelas

- 
- (1) Daughter of Eugenio Garza Lagüera.
  - (2) Sister-in-law of José Antonio Fernández Carbajal.
  - (3) Son-in-law of Eugenio Garza Lagüera.
  - (4) Wife of José Antonio Fernández Carbajal.
  - (5) Brother of José Calderón Rojas.
  - (6) Sister of Eugenio Garza Lagüera.
  - (7) Son of Consuelo Garza de Garza.
  - (8) Son of Max Michel Suberville.
  - (9) Brother of José Antonio Fernández Carbajal.
  - (10) Nephew of Max Michel Suberville.



**Table of Contents****Senior Management**

The names and positions of our current senior management and that of our principal sub-holding companies, their dates of birth and information on their principal business activities both within and outside of FEMSA are as follows:

**FEMSA**

José Antonio Fernández Carbajal	See Directors.	1987
<i>Chief Executive Officer</i>	Joined FEMSA:	1994
Javier Astaburuaga Sanjines	Appointed to current position: Born:	July 1959
<i>Executive Vice-President of Finance and Strategic Development</i>	Joined FEMSA:	1982
	Appointed to current position:	2006
	Business experience within FEMSA:	Joined FEMSA as a financial information analyst and later acquired experience in corporate development, administration and finance, held various senior positions at FEMSA Cerveza between 1993 and 2001, including Chief Financial Officer and for two years was FEMSA Cerveza's Director of Sales for the north region of Mexico until 2003 in which he was appointed FEMSA Cerveza's Co-Chief Executive Officer-Operations.
Federico Reyes García	Education: Born:	Holds a CPA degree from ITESM. September 1945
<i>Executive Vice-President of Corporate Development</i>	Joined FEMSA:	1999
	Appointed to current position:	2006
	Business experience within FEMSA:	Director of Corporate Development, 1992 and Chief Financial Officer from 1999 until 2006.
	Other business experience:	Served as Director of Corporate Staff at Grupo AXA and has extensive experience in the insurance sector, working eight years in Valores de Monterrey, S.A. de C.V., six of them as Chief Executive Officer
José González Ornelas	Education: Born:	Holds a degree in business and finance from ITESM April 1951
<i>Executive Vice President of Administration and Operative Control</i>	Joined FEMSA:	1973
	Appointed to current position:	2001
	Business experience within FEMSA:	Has held several managerial positions in FEMSA including Chief Financial Officer of FEMSA Cerveza, Director of Planning and Corporate Development of FEMSA and Chief Executive Officer of FEMSA Logística, S.A. de C.V.
	Education:	Holds a CPA degree from UANL and has post-graduate studies in business administration from the Instituto Panamericano de Alta Dirección de Empresa

(IPADE)

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Alfonso Garza Garza	Born:	July 1962
<i>Executive Vice President of Human Resources</i>	Joined FEMSA:	1985
	Appointed to current position:	2005
	Directorships:	Member of the board of Coca-Cola FEMSA and Hospital San José Tec de Monterrey
	Business experience within FEMSA:	Has experience in several FEMSA business units and departments, including domestic sales, international sales, procurement and marketing, mainly at Cervecería Cuauhtémoc Moctezuma, S.A. de C.V and as Chief Executive Officer of FEMSA Empaques
	Education:	Holds a degree in Industrial Engineering from ITESM and an MBA from IPADE
Carlos Aldrete Ancira	Born:	August 1956
<i>General Counsel and Secretary</i>	Joined FEMSA:	1979
	Appointed to current position:	1996
	Directorships:	
	Business experience within FEMSA:	Secretary of the Board of directors of FEMSA and secretary of the board of directors of all of the sub-holding companies
	Education:	Extensive experience in international business and financial transactions, debt issuances and corporate restructurings and expertise in securities and private mergers and acquisitions law
		Holds a law degree from the UANL and a masters degree in Comparative Law from the College of Law of the University of Illinois
<b>FEMSA Cerveza</b>		
Jorge Luis Ramos Santos	Born:	December 1952
<i>Chief Executive Officer</i>	Joined FEMSA:	1996
	Appointed to current position:	2006
	Business experience within FEMSA:	Director of Human Resources of FEMSA Cerveza from 1996 until 2000 and Director of Sales for the south region from 2000 until 2003. He acted as Co-Chief Executive Officer-Sales of FEMSA Cerveza from 2003 until his appointment to his current position
	Education:	Holds a bachelor's degree from ITESM and an MBA from the Wharton Business School.
<b>Coca-Cola FEMSA</b>		
Carlos Salazar Lomelín	Born:	April 1951
<i>Chief Executive Officer</i>	Joined FEMSA:	1973
	Appointed to current position:	2000

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Business experience within FEMSA:	Has held managerial positions in several subsidiaries of FEMSA, including Grafo Regia, S.A. de C.V. and Plásticos Técnicos Mexicanos, S.A. de C.V., served as Chief Executive Officer of FEMSA Cerveza, where he also held various management positions in the Commercial Planning and Export divisions
Education:	Holds a bachelor's degree in economics from ITESM, and is engaged in postgraduate studies in business administration and economic development in Italy

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Héctor Treviño Gutiérrez	Born:	August 1956
<i>Chief Financial Officer</i>	Joined FEMSA:	1981
	Appointed to current position:	1993
	Business experience within FEMSA:	Has held managerial positions in the international financing, financial planning, strategic planning and corporate development areas of FEMSA
	Education:	Holds a degree in chemical engineering from ITESM and an MBA from the Wharton Business School

**FEMSA Comercio**

Eduardo Padilla Silva	Born:	January 1955
<i>Chief Executive Officer</i>	Joined FEMSA:	1997
	Appointed to current position:	2003
	Business experience within FEMSA:	Director of Planning and Control of FEMSA from 1997 to 2000 and Chief Executive Officer, Strategic Business Division from 2000 until 2003
	Other business experience:	Had a 20-year career in Alfa, S.A.B. de C.V., culminating with a ten-year tenure as Chief Executive Officer of Terza, S.A. de C.V., major areas of expertise include operational control, strategic planning and financial restructuring
	Education:	Holds a degree in mechanical engineering from ITESM and an MBA from Cornell University

**Compensation of Directors and Senior Management**

The compensation of Directors is approved at the annual ordinary general shareholders meeting. For the year ended December 31, 2006, the aggregate compensation paid to our directors was approximately Ps. 4.9 million.

For the year ended December 31, 2006, the aggregate compensation paid to executive officers and senior management of FEMSA and its subsidiaries was approximately Ps. 988 million. Aggregate compensation includes bonuses we paid to certain members of senior management and payments in connection with the EVA stock incentive plan described below. Our senior management and executive officers participate in our benefit plan and post-retirement medical services plan on the same basis as our other employees. Members of our board of directors do not participate in our benefit plan and post-retirement medical services plan, unless they are retired employees of our company. As of December 31, 2006, amounts set aside or accrued for all employees under these retirement plans were Ps. 5,785 million, of which Ps. 2,713 million is already funded.

**Stock Incentive Plan**

From 1998 until 2003, we, along with our subsidiaries, had a five-year stock incentive plan for the benefit of our executive officers. Under the terms of the stock incentive plan, during the years 1999 through 2003, certain of our executive officers were selected to receive a special cash bonus, which was used to obtain a stock grant. Each year, our Chief Executive Officer, together with the chief executive officers and corporate practices committees of our sub-holding companies, selected the executive officers eligible to participate in the stock incentive plan and determined the amount of the special bonus, based on each executive officer's level of responsibility and corporate achievements during the prior year.

The stock grants were administrated by certain trusts for the benefit of the selected executive officers. Every year a new administrative trust was formed to manage the stock grants acquired in that particular year. Under the terms of the stock incentive plan, each time a special bonus was assigned to an executive officer, the executive officer contributed the special bonus received to the administrative trust in exchange for a stock grant, as





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etermined annually by us. Each administrative trust is managed by a technical committee formed by executives of our company and is governed by Mexican law.

A stock grant entitles an executive officer to receive BD Units or, in the case of officers of Coca-Cola FEMSA, a specified proportion of BD Units and Series L Shares of Coca-Cola FEMSA, which will be acquired by the respective administrative trust in the open market, using the special bonus contributed by each executive officer. Under the terms of the stock incentive plan, the ownership of the BD Units and, in its case, the Series L Shares of Coca-Cola FEMSA, will vest at a rate per year equivalent to the number of BD Units and, as applicable, Coca-Cola FEMSA Series L Shares, which can be acquired with 20% of such stock grant.

As of May 31, 2007, four administrative trusts, which administer the stock incentive plan, hold a total of 3,492,039 FEMSA BD Units (which amount reflects our three-for-one stock split in May 2007) and 353,930 Series L Shares of Coca-Cola FEMSA, each representing 0.02% and 0.13% of the total number of shares outstanding of FEMSA and of Coca-Cola FEMSA, respectively.

### **EVA Stock Incentive Plan**

In 2005, we along with our subsidiaries, commenced a new three-year stock incentive plan for the benefit of our executive officers, which we refer to as the EVA stock incentive plan. This new plan replaced the stock incentive plan described above and was developed using as the main metric for evaluation the Economic Value Added, or EVA, framework developed by Stern Stewart & Co., a compensation consulting firm. Under the EVA stock incentive plan, eligible executive officers are entitled to receive a special cash bonus, which will be used to purchase a stock grant.

Under this plan, each year, our Chief Executive Officer in conjunction with our board of directors, together with the chief executive officer of the respective sub-holding company, determines the amount of the special cash bonus used to purchase the stock grant. This amount is determined based on each executive officer's level of responsibility and based on the EVA generated by Coca-Cola FEMSA or FEMSA, as applicable.

The stock grants are administered by a trust for the benefit of the selected executive officers. Under the EVA stock incentive plan, each time a special bonus is assigned to an executive officer, the executive officer contributes the special bonus received to the administrative trust in exchange for a stock grant. Pursuant to the plan, the administrative trust acquires BD Units of FEMSA or, in the case of officers of Coca-Cola FEMSA, a specified proportion of publicly traded local shares of FEMSA and Series L Shares of Coca-Cola FEMSA on the Mexican Stock Exchange using the special bonus contributed by each executive officer. The ownership of the publicly traded local shares of FEMSA and, in the case of Coca-Cola FEMSA executives, the Series L Shares of Coca-Cola FEMSA vests upon the executive officer holding a stock grant each year over the next five years following the date of receipt of the stock grant, at a rate per year equivalent to 20% of the number of publicly traded local shares of FEMSA and Series L Shares of Coca-Cola FEMSA.

As of May 31, 2007, the trust that manages the EVA stock incentive plan holds a total of 5,670,291 FEMSA BD Units (which amount reflects our three-for-one stock split in May 2007) and 1,110,424 Series L Shares of Coca-Cola FEMSA, each representing 0.03% and 0.06% of the total number of shares outstanding of FEMSA and of Coca-Cola FEMSA, respectively.

### **Insurance Policies**

We maintain life insurance policies for all of our employees. These policies mitigate the risk of having to pay death benefits in the event of an industrial accident. We maintain a directors and officers' insurance policy covering all directors and certain key executive officers for liabilities incurred in their capacities as directors and officers.

### **Ownership by Management**

Several of our directors are participants of a voting trust. Each of the trust participants of the voting trust is deemed to have beneficial ownership with shared voting power over the shares deposited in the voting trust. As of

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May 31, 2007, 6,914,592,885 Series B Shares representing 74.78% of the outstanding Series B Shares were deposited in the voting trust. See Item 7. Major Shareholders and Related Party Transactions.

The following table shows the Series B Shares, Series D-B Shares and Series D-L Shares as of May 31, 2007 beneficially owned by our directors who are participants in the voting trust, other than the shares deposited in the voting trust:

Beneficial Owner	Series B		Series D-B		Series D-L	
	Shares	Percent of Class	Shares	Percent of Class	Shares	Percent of Class
Eugenio Garza Lagüera	13,440,804	0.15%	26,654,808	0.62%	26,654,808	0.62%
José Calderón Rojas	7,491,102	0.08	14,976,204	0.35	14,976,204	0.35
Consuelo Garza de Garza	69,401,775	0.75	12,754,950	0.30	12,754,950	0.30
Max Michel Suberville	5,151,345	0.06	10,302,690	0.24	10,302,690	0.24
Alberto Bailleres	8,658,381	0.09	11,129,112	0.25%	11,129,112	0.25%

To our knowledge, no other director or officer is the beneficial owner of more than 1% of any class of our capital stock.

**Board Practices**

Our bylaws state that the board of directors will meet at least once every three months following the end of each quarter to discuss our operating results and the advancement in the achievement of strategic objectives. Our board of directors can also hold extraordinary meetings. See Item 10. Additional Information Bylaws.

Under our bylaws, directors serve one-year terms although they continue in office even after the term for which they were appointed ends for up to 30 calendar days, as set forth in article 24 of Mexican Securities Law. None of our directors or senior managers of our subsidiaries has service contracts providing for benefits upon termination of employment.

Our board of directors is supported by committees, which are working groups that analyze issues and provide recommendations to the board of directors regarding their respective areas of focus. The executive officers interact periodically with the committees to address management issues. The following are the three committees of the board of directors:

*Audit Committee.* The Audit Committee works under internal regulations (Charters) that are approved by the Board of Directors. The Audit Committee is responsible for (1) reviewing the accuracy and integrity of quarterly and annual financial statements in accordance with accounting, internal control and auditing requirements, (2) for the appointment, compensation, retention and oversight of the independent auditor, who reports directly to the Audit Committee, (3) reviewing related party transactions other than in the ordinary course of our business and (4) identifying and following-up on contingencies and legal proceedings. The Audit Committee has implemented procedures for receiving, retaining and addressing complaints regarding accounting, internal control and auditing matters, including the submission of confidential, anonymous complaints from employees regarding questionable accounting or auditing matters. To carry out its duties, the Audit Committee may hire independent counsel and other advisors. As necessary, the company compensates the independent auditor and any outside advisor hired by the Audit Committee and provides funding for ordinary administrative expenses incurred by the Audit Committee in the course of its duties. The current Audit Committee members are: Alexis E. Rovzar de la Torre (Chairman), José Manuel Canal Hernando (Financial Expert), Francisco Zambrano Rodríguez and Alfonso González Migoya. Each member of the Audit Committee is an independent director, as required by the Mexican Securities Market Law and applicable New York Stock Exchange listing standards. The Secretary of the Audit Committee is José González Ornelas, head of FEMSA's internal audit department.

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*Finance Committee.* Responsibilities include (1) evaluating the investment and financing policies proposed by the Chief Executive Officer; (2) furnishing an opinion on the soundness of the annual budget and ensuring the implementation of the budget and any proposed strategic plan; and (3) identifying risk factors to which the corporation is exposed, as well as evaluating its management policies. The current Finance and Planning Committee members are: Ricardo Guajardo Touché (chairman), Alfredo Livas Cantú, Federico Reyes García, Robert E. Denham and Javier Fernández Carbajal. Javier Astaburuaga Sanjines is the appointed secretary of this committee.

*Corporate Practices Committee.* Under the Mexican Securities Law enacted in 2006, listed stock companies no longer have a statutory examiner. Instead, the functions previously performed by the statutory examiner are vested in the newly created Corporate Practices Committee, together with the Audit Committee. The Corporate Practices Committee, which consists of independent directors, is responsible for preventing or reducing the risk of performing operations that could damage the value of our company or that benefit a particular group of shareholders. The committee may call a shareholders' meeting and include matters on the agenda for that meeting that it may deem appropriate, approve policies on the use of our company's assets or related party transactions, approve the compensation of the chief executive officer and relevant officers and support our board of directors in the elaboration of reports on accounting practices. The chairman of the Corporate Practices Committee is Lorenzo H. Zambrano. The additional members include: Carlos Salguero and Helmut Paul. The Secretary of the Corporate Practices Committee is Alfonso Garza Garza.

**Employees**

As of December 31, 2006, our headcount by geographic region was as follows: 64,583 in Mexico, 4,962 in Central America, 7,955 in Colombia, 7,597 in Venezuela, 9,330 in Brazil and 3,343 in Argentina. We include in headcount employees of third party distributors who we do not consider to be our employees. The table below sets forth headcount for the years ended December 31, 2006, 2005 and 2004:

Sub-holding company	Headcount for the Year Ended December 31,							
	2006			2005			2004	
	Non-Union	Union	Total	Non-Union	Union	Non-Union	Union	
Coca-Cola FEMSA <sup>(1)</sup>	31,695	24,987	56,682	32,632	23,003	32,648	23,590	
FEMSA Cerveza	13,426	10,570	23,996	11,765	8,049	11,006	8,742	
FEMSA Comercio <sup>(2)</sup>	4,072	7,380	11,452	3,863	5,371	3,100	4,706	
Other	1,978	3,662	5,640	1,943	4,105	1,716	2,709	
Total	51,171	46,599	97,770	50,203	40,528	48,470	39,747	

(1) Includes employees of third party distributors who we do not consider to be our employees of 16,745, 16,421 and 16,182 in 2006, 2005, and 2004, respectively.

(2) Does not include non-management store employees, who are employed directly by each individual store.

As of December 31, 2006, our subsidiaries had entered into 398 collective bargaining or similar agreements with personnel employed at our operations. Each of the labor unions in Mexico is associated with one of 10 different national Mexican labor organizations. In general, we have a good relationship with the labor unions throughout our operations, except for in Colombia and Venezuela, which are the subject of significant labor-related litigation. See Item 8. Financial Information Legal Proceedings Coca-Cola FEMSA. The agreements applicable to our Mexican operations generally have an indefinite term and provide for an annual salary review and for review of other terms and conditions, such as fringe benefits, every two years.

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The table below sets forth the number of collective bargaining agreements and unions for our employees:

**Collective Bargaining Labor Agreements Between**

**Sub-holding Companies and Unions**

**As of December 31, 2006**

<b>Sub-holding Company</b>	<b>Collective Bargaining Agreements</b>	<b>Labor Unions</b>
Coca-Cola FEMSA	96	44
FEMSA Cerveza	149	11
FEMSA Comercio <sup>(1)</sup>	78	4
Others	75	10
<b>Total</b>	<b>398</b>	<b>69</b>

(1) Does not include non-management store employees, who are employed directly by each individual store.

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The following table identifies each owner of more than 5% of any class of our shares known to the company as of May 31, 2007. Except as described below, we are not aware of any holder of more than 5% of any class of our shares. Only the Series B Shares have full voting rights under our bylaws.

**Ownership of Capital Stock as of June 2007**

Shareholder	Series B Shares <sup>(1)</sup>		Series D-B Shares <sup>(2)</sup>		Series D-L Shares <sup>(3)</sup>		Total Shares of FEMSA Common Stock
	Shares	Percent	Shares	Percent	Shares	Percent	
	Owned	of Class	Owned	of Class	Owned	of Class	
Technical Committee and Trust Participants under the Voting Trust <sup>(4)</sup>	6,914,592,885	74.78%	0	0%	0	0%	38.64%

(1) As of May 31, 2007, there were 9,246,420,270 Series B Shares outstanding.

(2) As of May 31, 2007, there were 4,322,355,540 Series D-B Shares outstanding.

(3) As of May 31, 2007, there were 4,322,355,540 Series D-L Shares outstanding.

(4) As a consequence of the voting trust's internal procedures, the following trust participants are deemed to have beneficial ownership with shared voting power over those same deposited shares: BBVA Bancomer Servicios, S.A., as Trustee under Trust No. F/25078-7 (controlled by Max Michel Suberville), Eugenio Garza Lagüera, Paulina Garza Lagüera Gonda, Bárbara Garza de Braniff, Mariana Garza Lagüera Gonda, Eva Gonda Rivera, Eva Maria Garza Lagüera Gonda, Consuelo Garza Lagüera de Garza, Alfonso Garza Garza, Patricio Garza Garza, Juan Carlos Garza Garza, Eduardo Garza Garza, Eugenio Garza Garza, Alberto Bailleres González, Maria Teresa Gual Aspe de Bailleres, Inversiones Bursátiles Industriales, S.A. de C.V. (controlled by Eugenio Garza Lagüera), Corbal, S.A. de C.V. (controlled by Alberto Bailleres Gonzalez), Magdalena Michel de David, Alepage, S.A. (controlled by Consuelo Garza Lagüera de Garza), BBVA Bancomer Servicios, S.A. as Trustee under Trust No. F/29013-0 (controlled by the estate of José Calderón Ayala, late father of José Calderón Rojas), Max Michel Suberville, Max David Michel, Juan David Michel, Monique David de VanLathem, Renee Michel de Guichard, Magdalena Guichard Michel, Rene Guichard Michel, Miguel Guichard Michel, Graciano Guichard Michel, Juan Guichard Michel, Franca Servicios, S.A. de C.V. (controlled by the estate of José Calderón Ayala, late father of José Calderón Rojas), BBVA Bancomer Servicios, S.A., as Trustee under Trust No. F/29490-0 (controlled by Alberto, Susana and Cecilia Bailleres), BBVA Bancomer Servicios, S.A., as Trustee under Trust No. F/710004 (controlled by Magdalena Michel de David) and BBVA Bancomer Servicios, S.A., as Trustee under Trust No. F/700005 (controlled by Renee Michel de Guichard).

As of May 31, 2007, there were 25 holders of record of ADSs in the United States, which represented approximately 53% of our outstanding BD Units. Since a substantial number of ADSs are held in the name of nominees of the beneficial owners, including the nominee of The Depository Trust Company, the number of beneficial owners of ADSs is substantially greater than the number of record holders of these securities.

**Related-Party Transactions****Voting Trust**

The trust participants, who are our principal shareholders, agreed in April 1998 to deposit a majority of their shares, which we refer to as the trust assets, of FEMSA into the voting trust, and later entered into an amended agreement on August 8, 2005, following the substitution of Banco Inxev, S.A. as trustee to the voting trust. The primary purpose of the voting trust is to permit the trust assets to be voted as a block, in accordance with the instructions of the technical committee. The trust participants are separated into seven trust groups and the



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technical committee is comprised of one representative appointed by each trust group. The number of B Units corresponding with each trust group (the proportional share of the shares deposited in the trust of such group) determines the number of votes that each trust representative has on the technical committee. Most matters are decided by a simple majority of the trust assets.

The trust participants agreed to certain transfer restrictions with respect to the trust assets. The trust is irrevocable, for a term that will conclude on May 31, 2013 (subject to additional five-year renewal terms), during which time, trust assets may be transferred by trust participants to spouses and immediate family members and, subject to certain conditions, to companies that are 100% owned by trust participants, which we refer to as the permitted transferees, provided in all cases that the transferee agrees to be bound by the terms of the voting trust. In the event that a trust participant wishes to sell part of its trust assets to someone other than a permitted transferee, the other trust participants have a right of first refusal to purchase the trust assets that the trust participant wishes to sell. If none of the trust participants elects to acquire the trust assets from the selling trust participant, the technical committee will have a right to nominate (subject to the approval of technical committee members representing 75% of the trust assets, excluding trust assets that are the subject of the sale) a purchaser for such trust assets. In the event that none of the trust participants or a nominated purchaser elects to acquire trust assets, the selling trust participant will have the right to sell the trust assets to a third party on the same terms and conditions that were offered to the trust participants. Acquirors of trust assets will only be permitted to become parties to the voting trust upon the affirmative vote by the technical committee of at least 75% of the trust shares, which must include trust shares represented by at least three trust group representatives. In the event that a trust participant holding a majority of the trust assets elects to sell its trust assets, the other trust participants have tag along rights that will enable them to sell their trust assets to the acquiror of the selling trust participant's trust assets.

Because of their ownership of a majority of the Series B Shares, the trust participants may be deemed to control our company. Other than as a result of their ownership of the Series B Shares, the trust participants do not have any voting rights that are different from those of other shareholders.

### **Interest of Management in Certain Transactions**

The following is a summary of transactions we have entered into with entities for which members of our board of directors or management serve as a member of the board of directors or management. Each of these transactions was entered into in the ordinary course of business, and we believe each is on terms comparable to those that could be obtained in arm's length negotiations with unaffiliated third parties. Under our by-laws, transactions entered with related parties not in the ordinary course of business are subject to the approval of our board of directors, subject to the prior opinion of the Audit Committee.

Until 2004, we, along with certain of our subsidiaries, engaged in financial and insurance coverage transactions, including entering into loans and credit line facilities, with subsidiaries of BBVA Bancomer, a financial services holding company of which Ricardo Guajardo Touché, who is also a director of FEMSA, was the chairman of the board of directors until the fourth quarter of 2004 and is currently a director of, and of which José Antonio Fernández Carbajal, our Chairman and Chief Executive Officer, and Alberto Bailleres, one of our directors, are directors. These transactions include the following: (1) BBVA Bancomer was the administrative agent and was one of the lenders in a Ps. 1,728 million credit agreement entered into by FEMSA Comercio in 2004; (2) BBVA Bancomer was the lender in a Ps. 1,155 million credit agreement entered into with FEMSA Cerveza in 2004; (3) BBVA Bancomer was the lender in a Ps. 1,636 million credit agreement entered into with FEMSA Cerveza in 2003; (4) BBVA Bancomer was one of the two lenders in a Ps. 1,762 million credit agreement entered into with FEMSA in 2004; and (5) BBVA Bancomer and its affiliates are also a lender under a term loan facility and a purchaser of *certificados bursátiles* issued in Mexico by Coca-Cola FEMSA in connection with the acquisition of Panamco.

We maintain an insurance policy covering auto insurance and medical expenses for executives issued by Grupo Nacional Provincial, S.A., an insurance company of which the chairman of the board and chief executive officer is Alberto Bailleres, one of our directors. The aggregate amount of premiums paid under these policies was approximately Ps. 39 million, Ps. 52 million, and Ps. 84 million in 2006, 2005 and 2004, respectively.

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In 2006, FEMSA Comercio in its ordinary course of business, purchased Ps. 997 million, Ps. 916 million, and Ps. 813 million in 2006, 2005 and 2004, respectively, in baked goods and snacks for its stores from subsidiaries of Grupo Bimbo, S.A.B. de C.V., of which the chairman of the board is Roberto Servitje, a director of FEMSA. These purchases were entered into in the ordinary course of business, and we believe they were made on terms comparable to those that could be obtained in arm's length negotiations with unaffiliated third parties.

José Antonio Fernández Carbajal, Ricardo Guajardo Touché and Lorenzo H. Zambrano, who are directors of FEMSA, and Eva Garza de Fernández, who is an alternate director of FEMSA, are also members of the board of directors of ITESM, which is a prestigious university in Monterrey, Mexico that routinely receives donations from FEMSA and its subsidiaries.

### **Business Transactions between Coca-Cola FEMSA and The Coca-Cola Company**

Coca-Cola FEMSA regularly engages in transactions with The Coca-Cola Company and its affiliates. Coca-Cola FEMSA purchases all of its concentrate requirements for Coca-Cola trademark beverages from The Coca-Cola Company. Total payments by Coca-Cola FEMSA to The Coca-Cola Company for concentrates were approximately Ps. 9,298 million, Ps. 8,328 million, and Ps. 7,767 million in 2006, 2005 and 2004, respectively. Coca-Cola FEMSA and The Coca-Cola Company pay and reimburse each other for marketing expenditures. The Coca-Cola Company also contributes to Coca-Cola FEMSA's refrigeration equipment investment program. Coca-Cola FEMSA received contributions to its marketing expenses, which include its refrigeration equipment investment program, of Ps. 1,164 million, Ps. 1,106 million, and Ps. 1,018 million in 2006, 2005 and 2004, respectively.

In Argentina, Coca-Cola FEMSA also purchases a portion of its plastic ingot requirements for producing plastic bottles and all of its returnable bottle requirements from Embotelladora del Atlántico S.A., a local subsidiary of Embotelladora Andina, S.A., a Coca-Cola bottler with operations in Argentina, Chile and Brazil in which The Coca-Cola Company has a substantial interest.

In connection with the acquisition of Panamco, subsidiaries of The Coca-Cola Company made specified undertakings to support and facilitate the Panamco acquisition for the benefit of Coca-Cola FEMSA. In consideration for these undertakings, Coca-Cola FEMSA made certain undertakings for the benefit of The Coca-Cola Company and its subsidiaries, including indemnity obligations with respect to specified matters relating to the accuracy of disclosure and the compliance with applicable law by Coca-Cola FEMSA's board of directors and the board of directors of Panamco and undertakings to take specified actions and refrain from specified others to facilitate the ability of The Coca-Cola Company to receive favorable tax treatment in connection with its participation in the acquisition. In connection with the execution of the acquisition agreement for Panamco, The Coca-Cola Company and FEMSA memorialized their understandings relating to specified operational and business issues that may affect Coca-Cola FEMSA following completion of the acquisition. A summary of these understandings is set forth under Item 10. Additional Information Material Contracts The Coca-Cola Memorandum.

On December 19, 2006, Coca-Cola FEMSA and The Coca-Cola Company announced an agreement with the controlling shareholders of Jugos del Valle to conduct a public tender offer in Mexico for up to 100% of the outstanding public shares of Jugos del Valle. If the tender offer is successfully completed, Coca-Cola FEMSA and Jugos del Valle would jointly control Jugos del Valle. See Item 5. Operating and Financial Review and Prospectus Recent Developments.

On June 25, 2007, the *Comisión Federal de Competencia* (CFC), or the Mexican Antitrust Commission, notified us of its decision to object to the acquisition of Jugos del Valle. We intend to consider our options with respect to the transaction, which may include seeking a reconsideration of the decision.

## **ITEM 8. FINANCIAL INFORMATION**

### **Consolidated Financial Statements**

See pages F-1 through F-63, incorporated herein by reference.



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### **Dividend Policy**

For a discussion of our dividend policy, see Item 3. Key Information Dividends and Item 10. Additional Information.

### **Legal Proceedings**

We are party to various legal proceedings in the ordinary course of business. Other than as disclosed in this annual report, we are not currently involved in any litigation or arbitration proceeding, including any proceeding that is pending or threatened of which we are aware, which we believe will have, or has had, a material adverse effect on our company. Other legal proceedings that are pending against or involve us and our subsidiaries are incidental to the conduct of our and their business. We believe that the ultimate disposition of such other proceedings individually or on an aggregate basis will not have a material adverse effect on our consolidated financial position or results of operations.

### **Coca-Cola FEMSA**

#### **Mexico**

##### *Antitrust Matters*

During 2000, the *Comisión Federal de Competencia* (the Mexican Antitrust Commission), pursuant to complaints filed by PepsiCo. and certain of its bottlers in Mexico, started an investigation of The Coca-Cola Company and its bottlers. Later in 2002, the Mexican Antitrust Commission determined that The *Coca-Cola* Company's bottlers engaged in monopolistic practices through exclusivity arrangements with certain retailers. The Mexican Antitrust Commission did not impose any fines, but ordered The *Coca-Cola* Company's bottlers, including certain of Coca-Cola FEMSA's Mexican subsidiaries, to abstain from entering into any exclusivity arrangement with retailers that stock soft drink bottles of up to 2.0-liters. Coca-Cola FEMSA, along with other *Coca-Cola* bottlers, appealed the resolution rendered in February 2002 by a *Recurso de Reconsideración* (Review Recourse) that was presented before the Mexican Antitrust Commission. The Mexican Antitrust Commission confirmed its original determination and issued a confirmatory resolution in July 2002. Coca-Cola FEMSA and its Mexican operating subsidiaries appealed this resolution before a Mexican federal court by initiating several *juicios de amparo* (appeals based on the violation of constitutional rights) and obtained favorable final decisions not subject to appeal. Under these judicial decisions, the resolution was declared null and void and the Mexican Antitrust Commission was ordered to issue a new resolution.

The case was inactive until May 2005, when the Mexican Antitrust Commission ordered the reopening of the proceeding and initiated the period for the filing of pleadings. Coca-Cola FEMSA subsequently filed its pleadings. In the proceeding, the Mexican Antitrust Commission determined, as in its first instance resolution, that the Coca-Cola bottlers engaged in monopolistic practices and (1) ordered the immediate suspension of such practices of alleged exclusivity arrangements and (2) imposed a fine of approximately Ps. 63.2 million.

Coca-Cola FEMSA filed an *amparo* proceeding challenging this rule in Mexican federal court, and an order was issued in its favor that granted protection against the resolution of the Mexican Antitrust Commission. The Mexican Antitrust Commission and the plaintiffs appealed this order to a Mexican Federal Court, which determined that the *Suprema Corte de Justicia de la Nación* (Mexican Supreme Court) should render a final decision on this matter. The result of such judgment is expected in the following coming months.

In March 2003, in a separate proceeding, the Mexican Antitrust Commission started an investigation involving The Coca-Cola Company, Coca-Cola FEMSA and certain other Coca-Cola bottlers due to complaints filed by some retailers and Ajemex, S.A. de C.V. (Big Cola). In September 2003, the Mexican Antitrust Commission requested certain *Coca-Cola* bottlers, including some of Coca-Cola FEMSA's Mexican subsidiaries, to provide information. Coca-Cola FEMSA initiated *amparo* proceedings, and a Mexican federal court issued a final ruling stating that the requests for information were unconstitutional. In August 2004, however, as a result of the investigation, the Mexican Antitrust Commission issued several *Oficios de Presunta Responsabilidad*

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(Statements of Charges) asserting that Coca-Cola FEMSA and its Mexican operating subsidiaries, as well as other bottlers, engaged in monopolistic practices and requested additional information. Coca-Cola FEMSA replied to the *Oficios de Presunta Responsabilidad* (Statements of Charges) by offering certain evidence, including expert witness reports, which were rejected by the Mexican Antitrust Commission. The Mexican Antitrust Commission issued a resolution that determined Coca-Cola FEMSA engaged in certain monopolistic practices and ordered it to abstain from engaging in such practices and imposed a fine of Ps. 63.2 million. Coca-Cola FEMSA initiated *amparo* proceedings against such first instance resolution, which are currently under review. We believe the resolution is without merit and intends to defend itself in this matter.

Thereafter, the investigated companies filed an appeal before the Mexican Antitrust Commission, which affirmed its prior resolution. Coca-Cola FEMSA subsequently challenged the resolution in Mexican federal court, which determined that the *Suprema Corte de Justicia de la Nación* (the Mexican Supreme Court) should render a final decision on this matter. A final ruling is expected within approximately the next 6 months.

We believe these assessments are without merit, however, we cannot give any assurances that any action taken as a result of these investigations will not negatively affect the company in the future.

## **Central America**

### *Antitrust Matters in Costa Rica*

During August 2001, the *Comisión para Promover la Competencia* in Costa Rica (Costa Rican Antitrust Commission), pursuant to a complaint filed by PepsiCo. and its bottler in Costa Rica, initiated an investigation of the sales practices of The Coca-Cola Company and Coca-Cola FEMSA's Costa Rican subsidiary for alleged monopolistic practices in retail distribution, including sales exclusivity arrangements. A ruling from the Costa Rican Antitrust Commission was issued in July 2004, which found the company engaged in monopolistic practices with respect to exclusivity arrangements, pricing and the sharing of refrigeration equipment under certain limited circumstances and imposed a US\$ 130,000 fine. Coca-Cola FEMSA's appeal of the Costa Rican Antitrust Commission's ruling was recently dismissed. Coca-Cola FEMSA has filed judicial proceedings challenging the ruling of the Costa Rican Antitrust Commission and the process is still pending in court. We do not believe that this matter will have a material adverse effect on its financial condition or results of operations.

In November, 2004, Ajecen del Sur S.A., the bottler of Big Cola in Costa Rica, filed a complaint before the Costa Rican Antitrust Commission related to monopolistic practices in retail distribution and exclusivity agreements against The Coca-Cola Company and Coca-Cola FEMSA's Costa Rican subsidiary. The Costa Rican Antitrust Commission has decided to pursue an investigation. The period for gathering of evidence ended in August 2006, and the final arguments have been filed. Coca-Cola FEMSA is waiting for the final resolution to be issued by the Costa Rican Antitrust Commission, which it expects to be issued at the end of March 2007.

### *Tax Matters in Costa Rica*

In September 2004, Coca-Cola FEMSA's Costa Rican subsidiary received notice of certain tax claims asserted by the Costa Rican tax authorities to pay taxes on sales of carbonated soft drinks from April 2002 through July 2003. These claims currently total approximately US\$ 12 million. In previous years, Coca-Cola FEMSA's Costa Rican subsidiary had been required to pay similar taxes, however, due to favorable final decisions Coca-Cola FEMSA received on appeals that it filed, it was not required to pay these taxes. Coca-Cola FEMSA has initiated a legal action against the current assessment by the Costa Rican tax authorities, which is currently under review. We believe this assessment is without merit.

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### **Colombia**

#### *Labor Matters*

During July 2001, a labor union and several individuals from the Republic of Colombia filed a lawsuit in the U.S. District Court for the Southern District of Florida against certain of Coca-Cola FEMSA's subsidiaries. In the complaint, the plaintiffs alleged that the subsidiaries of the company acquired in the Panamco acquisition engaged in wrongful acts against the labor union and its members in Colombia, including kidnapping, torture, death threats and intimidation. The complaint alleges claims under the U.S. Alien Tort Claims Act, Torture Victim Protection Act, Racketeer Influenced and Corrupt Organizations Act and state tort law and seeks injunctive and declaratory relief and damages of more than US\$ 500 million, including treble and punitive damages and the cost of the suit, including attorney fees. Coca-Cola FEMSA filed a motion to dismiss the complaint for lack of subject matter and personal jurisdiction. The court denied the motion to dismiss and the complaint based on jurisdictional grounds. The court also granted the motion to dismiss with respect to all of the claims in the lawsuit. Plaintiffs initially filed a motion of appeal and subsequently moved to stay the appellate proceedings. We believe this lawsuit is without merit and intends to defend itself in this matter.

### **Venezuela**

#### *Tax Matters*

In 1999, certain of Coca-Cola FEMSA's Venezuelan subsidiaries received notice of certain tax claims asserted by the Venezuelan tax authorities. These subsidiaries have taken the appropriate recourse against these claims at the administrative level as well as before the courts in Venezuela. The claims currently total approximately US\$ 15.6 million. The company has certain rights to indemnification from Venbottling Holding, Inc., a former shareholder of Panamco and The Coca-Cola Company, for a substantial portion of the claims. Coca-Cola FEMSA does not believe that the ultimate disposition of these cases will have a material adverse effect on its financial condition or results of operations.

#### *Labor and Distribution Matters*

Since 2001, Coca-Cola FEMSA's Venezuelan subsidiaries have been the subject of more than 400 claims and lawsuits by former independent distributors claiming alleged labor and severance rights owed to them at the time of the termination of their relationship with Coca-Cola FEMSA. As of December 31, 2006, the total amounts claimed by former distributors in respect of Coca-Cola FEMSA's Venezuela subsidiary were approximately US\$14.8 million. Notwithstanding the number of claims and the amounts involved, most of these claims have been filed by former distributors that either entered into release agreements with Coca-Cola FEMSA's subsidiaries at the time of their termination, and therefore Coca-Cola FEMSA believes have no rights for additional claims, or are claims that were filed after the expiration of the statute of limitations. These claims have been the subject of hearings in the Venezuelan National Assembly, which is requiring review of the claims by the Venezuelan Supreme Court. No decision has yet been issued.

### **Brazil**

#### *Antitrust Matters*

Several claims have been filed against Coca-Cola FEMSA by private parties, which are currently pending before the Brazilian Ministry of Law and Economics that allege anticompetitive practices by Coca-Cola FEMSA's Brazilian subsidiaries. The plaintiffs are Ragi (Dolly), a Brazilian producer of B Brands, and PepsiCo. Under Brazilian law, each of these claims could result in substantial monetary fines and other penalties. We believe each of the claims is without merit, and it intends to defend itself in these matters.

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**FEMSA Cerveza**

*Antitrust Matters*

On June 18, 2003, the Mexican Antitrust Commission disclosed its intention to launch an investigation (file number IO-05-2003) into the alleged beer industry practice of tied-customer arrangements. FEMSA Cerveza was among the brewers that received a request for information from the Mexican Antitrust Commission and responded by filing several amparo proceedings challenging the legality of the Commission's actions. Thus far, the Mexican federal courts have ruled on all of these proceedings, finding no proper support or validity with respect to the Mexican Antitrust Commission's request. As of the date of this annual report, the Mexican Antitrust Commission has not formally closed its investigation nor charged FEMSA Cerveza with any illegal behavior. However, FEMSA Cerveza cannot give any assurances that any action taken as a result of this investigation will not negatively affect FEMSA Cerveza's operations in the future.

On August 24, 2004, the Mexican Antitrust Commission disclosed that it was launching an investigation (file number DE-24-2005) into beer industry practices with respect to exclusivity arrangements within the beer industry, and we and FEMSA Cerveza were among the companies that received requests for information on September 15, 2004 from the Mexican Antitrust Commission. On October 7, 2004, we and FEMSA Cerveza filed amparo proceedings before the appropriate Mexican federal district courts to challenge the grounds of the Mexican Antitrust Commission's investigation and the requests for information. Concluding that we and FEMSA Cerveza unjustifiably failed to provide the information and documents requested by the Mexican Antitrust Commission, the Antitrust Commission imposed minor monetary fines on both us and FEMSA Cerveza, which challenged the corresponding resolutions.

In October 2005, as a result of its investigation, the Mexican Antitrust Commission issued an Oficio de Presunta Responsabilidad (Statement of Charges) asserting that FEMSA and FEMSA Cerveza had engaged in monopolistic practices. FEMSA and FEMSA Cerveza filed a rebuttal to such statement of charges and the proceedings are ongoing. Neither we nor FEMSA Cerveza can give any assurances that any action taken as a result of this investigation will not negatively affect us in the future.

**ITEM 9. THE OFFER AND LISTING**

**Description of Securities**

We have three series of capital stock, each with no par value:

Series B Shares;

Series D-B Shares; and

Series D-L Shares.

Series B Shares have full voting rights, and Series D-B and D-L Shares have limited voting rights. Prior to May 11, 2008, the shares of our company are not separable and may be transferred only in the following forms:

B Units, consisting of five Series B Shares; and

BD Units, consisting of one Series B Share, two Series D-B Shares and two Series D-L Shares.

At our annual general ordinary shareholders' meeting held on March 29, 2007, our shareholders approved a three-for-one stock split in respect all of our outstanding capital stock. Following the stock split, our total capital stock consists of 2,161,177,770 BD Units and 1,417,048,500 B Units. Our stock split also resulted in a three-for-one stock split our American Depositary Shares. The stock-split was conducted on a pro-rata basis in respect of all holders of our shares and all ADSs holders of record as of May 25, 2007, and the ratio of voting and non-voting shares was

maintained, thereby preserving our ownership structure as it was prior to the stock-split.

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On May 11, 2008, each Series D-B Share will automatically convert into one Series B Share with full voting rights, and each Series D-L Share will automatically convert into one Series L Share with limited voting rights. At that time:

the BD Units and the B Units will cease to exist and the underlying Series B Shares and Series L Shares will be separate; and

the Series B Shares and Series L Shares will be entitled to share equally in any dividend, and the dividend preferences of the Series D-B Shares and Series D-L Shares of 125% of any amount distributed in respect of each Series B Share existing prior to May 11, 2008 will be terminated.

The following table sets forth information regarding our capital stock as of May 31, 2007:

Class	Number	Percentage of Capital	Percentage of Voting
Series B Shares (no par value)	9,246,420,270	51.7%	100.0%
Series D-B Shares (no par value)	4,322,355,540	24.2	0.0
Series D-L Shares (no par value)	4,322,355,540	24.2	0.0
Total Shares	17,891,131,350	100.0	100.0
Units			
BD Units	2,161,177,770	60.4	23.4
B Units	1,417,048,500	39.6	76.6
Total Units	3,578,226,270	100.0	100.0

**Trading Markets**

Prior to May 11, 1998, there was no market for the BD Units, the B Units or any of our shares. Since May 11, 1998, ADSs representing BD Units have been listed on the New York Stock Exchange, and the BD Units and the B Units have been listed on the Mexican Stock Exchange. Each ADS represents 10 BD Units deposited under the deposit agreement with the ADS depository.

The New York Stock Exchange trading symbol for the ADSs is **FMX** and the Mexican Stock Exchange trading symbols are **FEMSA UBD** for the BD Units and **FEMSA UB** for the B Units.

Fluctuations in the exchange rate between the Mexican peso and the U.S. dollar have affected the U.S. dollar equivalent of the Mexican peso price of our shares on the Mexican Stock Exchange and, consequently, have also affected the market price of our ADSs. See Item 3. Key Information Exchange Rate Information.

**Trading on the Mexican Stock Exchange**

The Mexican Stock Exchange, located in Mexico City, is the only stock exchange in Mexico. Founded in 1907, it is organized as a corporation, the shares of which are held by 30 brokerage firms, that are exclusively authorized to trade on the exchange. Trading on the Mexican Stock Exchange takes place principally through automated systems and is open between the hours of 8:30 a.m. and 3:00 p.m. Mexico City time, each business day. Trades in securities listed on the Mexican Stock Exchange can also be effected off the exchange. The Mexican Stock Exchange operates a system of automatic suspension of trading in shares of a particular issuer as a means of controlling excessive price volatility, but under current regulations this system does not apply to securities such as the BD Units that are directly or indirectly (for example, in the form of ADSs) quoted on a stock exchange (including for these purposes the New York Stock Exchange) outside Mexico.

Settlement is effected two business days after a share transaction on the Mexican Stock Exchange. Deferred settlement, even by mutual agreement, is not permitted without the approval of the *Comisión Nacional Bancaria y de Valores* (the Mexican National Banking and Securities Commission) or CNBV. Most securities traded on the Mexican Stock Exchange, including ours, are on deposit with *S.D. Indeval, S.A. de C.V., Instituto para el Depósito de Valores*, a privately owned securities depository that acts as a clearinghouse for Mexican Stock Exchange transactions.



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The following tables set forth, for the periods indicated, the reported high, low and closing sale prices and the average daily trading volumes for the BD Units and B Units on the Mexican Stock Exchange and the reported high, low and closing sale prices and the average daily trading volumes for the ADSs on the New York Stock Exchange.

	BD Units <sup>(1)</sup>					Average Daily Trading Volume (Units)
	Nominal pesos			FX rate	Close US\$ <sup>(4)</sup>	
	High <sup>(2)</sup>	Low <sup>(2)</sup>	Close <sup>(3)</sup>			
<b>2002</b>	46.00	31.89	37.93	10.43	3.64	948,565
<b>2003</b>	44.68	33.50	41.48	11.24	3.69	1,011,052
<b>2004</b>	59.60	41.02	58.51	11.15	5.25	1,104,705
<b>2005</b>						
First Quarter	67.75	57.02	59.84	11.18	5.35	546,675
Second Quarter	64.13	55.89	64.13	10.77	5.95	936,520
Third Quarter	79.39	63.70	75.14	10.79	6.96	677,012
Fourth Quarter	77.96	70.09	77.08	10.63	7.25	614,653
<b>2006</b>						
First Quarter	100.72	77.06	99.45	10.90	9.13	849,706
Second Quarter	106.08	83.73	94.91	11.29	8.41	878,448
Third Quarter	109.33	88.60	106.76	10.98	9.72	597,854
Fourth Quarter	126.76	102.61	125.17	10.80	11.59	842,273
December	127.90	116.30	125.17	10.80	11.59	695,867
<b>2007</b>						
January	133.12	123.00	132.26	11.04	11.98	767,732
February	146.48	119.65	123.62	11.16	11.08	1,516,205
March	128.00	114.80	122.03	11.04	11.05	2,011,262
April	127.73	116.26	117.85	10.93	10.78	2,151,658
May	42.83 <sup>(5)</sup>	40.08 <sup>(5)</sup>	42.71 <sup>(5)</sup>	10.74	3.98 <sup>(5)</sup>	6,089,873 <sup>(6)</sup>
June <sup>(7)</sup>	43.52 <sup>(5)</sup>	42.00 <sup>(5)</sup>	42.26 <sup>(5)</sup>	10.81	3.91 <sup>(5)</sup>	3,615,491 <sup>(6)</sup>

(1) The prices and average daily trading volume for the BD Units were taken from Bloomberg.

(2) High and low closing prices for the periods presented.

(3) Closing price on the last day of the periods presented.

(4) Represents the translation from Mexican pesos to U.S. dollars of the closing price of the BD Units on the last day of the periods presented based on the noon buying rate for the purchase of U.S. dollars, as reported by the Federal Reserve Bank of New York on such date.

(5) Reflects 3-for-1 stock split, which was effective May 28, 2007 in respect of our BD Units

(6) Reflects increased trading volume as of May 28, 2007 as a result of our 3-for-1 stock split.

(7) Information from June 1 to June 15, 2007.





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	Nominal pesos			B Units <sup>(1)</sup>		Average Daily Trading Volume(Units)
	High <sup>(2)</sup>	Low <sup>(2)</sup>	Close <sup>(3)</sup>	FX rate	Close US\$ <sup>(4)</sup>	
<b>2002</b>	40.00	34.00	37.00	10.43	3.55	800
<b>2003</b>	40.90	33.70	38.70	11.24	3.44	2,278
<b>2004</b>	52.00	39.50	52.00	11.15	4.66	4,278
<b>2005</b>						
First Quarter	56.39	48.70	55.00	11.18	4.92	591
Second Quarter	58.24	50.11	51.15	10.77	4.75	991,861
Third Quarter	72.50	53.95	72.24	10.79	6.69	525
Fourth Quarter	71.25	65.00	65.00	10.63	6.12	195
<b>2006</b>						
First Quarter	90.00	69.00	90.00	10.90	8.26	214,962
Second Quarter	102.28	92.00	92.00	11.29	8.15	80,674
Third Quarter	100.00	91.00	100.00	10.98	9.11	825
Fourth Quarter	101.00	96.50	100.00	10.80	9.26	1,247
December	100.00	100.00	100.00	10.80	9.26	2,500
<b>2007</b>						
January	112.00	100.00	112.00	11.04	10.14	525
February	127.00	116.00	127.00	11.16	11.38	20,900
March	122.00	118.49	122.00	11.04	11.05	7,867
April	122.00	122.00	122.00	10.93	11.16	0
May	40.92 <sup>(5)</sup>	40.33 <sup>(5)</sup>	40.92 <sup>(5)</sup>	10.74	3.81 <sup>(5)</sup>	1,500 <sup>(6)</sup>
June <sup>(7)</sup>	42.00 <sup>(5)</sup>	41.00 <sup>(5)</sup>	41.70 <sup>(5)</sup>	10.81	3.86 <sup>(5)</sup>	2,167 <sup>(6)</sup>

- (1) The prices and average daily trading volume for the B Units were taken from Bloomberg.
- (2) High and low closing prices for the periods presented.
- (3) Closing price on the last day of the periods presented.
- (4) Represents the translation from Mexican pesos to U.S. dollars of the closing price of the B Units on the last day of the periods presented based on the noon buying rate for the purchase of U.S. dollars, as reported by the Federal Reserve Bank of New York on such date.
- (5) Reflects 3-for-1 stock split, which was effective May 28, 2007, in respect of our B Units.
- (6) Reflects increased trading volume as of May 28, 2007 as a result of our 3-for-1 stock split.
- (7) Information from June 1 to June 15, 2007.

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	ADSs <sup>(1)</sup>			Average Daily Trading Volume (ADSs)
	U.S. dollars			
	High <sup>(2)</sup>	Low <sup>(2)</sup>	Close <sup>(3)</sup>	
<b>2002</b>	49.21	33.80	36.42	229,017
<b>2003</b>	42.11	30.65	36.88	250,142
<b>2004</b>	52.93	37.01	52.61	282,296
<b>2005</b>				
First Quarter	60.88	51.05	53.55	296,533
Second Quarter	59.57	50.91	59.57	383,661
Third Quarter	73.75	59.32	69.92	357,092
Fourth Quarter	72.55	64.50	72.51	275,079
<b>2006</b>				
First Quarter	91.94	74.56	91.66	355,721
Second Quarter	96.99	73.22	83.72	509,811
Third Quarter	99.90	80.66	96.94	351,371
Fourth Quarter	117.50	95.35	115.76	328,252
December	118.88	105.50	115.76	353,710
<b>2007</b>				
January	120.54	112.10	120.07	349,990
February	134.25	105.25	110.58	676,775
March	116.37	102.45	110.39	594,777
April	116.40	106.22	107.69	666,381
May	39.91 <sup>(4)</sup>	36.79 <sup>(4)</sup>	39.84 <sup>(4)</sup>	1,030,187 <sup>(5)</sup>
June <sup>(6)</sup>	40.44 <sup>(4)</sup>	38.40 <sup>(4)</sup>	39.35 <sup>(4)</sup>	739,209 <sup>(5)</sup>

(1) Each ADS is comprised of 10 BD Units. Prices and average daily trading volume were taken from Bloomberg.

(2) High and low closing prices for the periods presented.

(3) Closing price on the last day of the periods presented.

(4) Prices reflect 3-for-1 stock split, which was effective in respect of our ADS on May 30, 2007.

(5) Reflects increased trading volume as of May 30, 2007 as a result of our 3-for-1 stock split.

(6) Information from June 1, 2007 to June 15, 2007.

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### ITEM 10. ADDITIONAL INFORMATION

#### Bylaws

The following is a summary of the material provisions of our bylaws and applicable Mexican law. For a description of the provisions of our bylaws relating to our board of directors and executive officers, see Item 6. Directors, Senior Management and Employees.

The Mexican Securities Law that came into effect in 2006 includes provisions that, among others, seek to improve the regulation of disclosure of information, minority shareholder rights and corporate governance. In addition, the Mexican Securities Law imposes further duties and liabilities on the members of the board of directors as well as on the relevant officers (such as a duty of loyalty and a duty of care). Likewise, under the Mexican Securities Law we were required to adopt specific amendments to our bylaws, which we carried out in 2006. The most significant of these amendments relate to the following:

change in our corporate name to reflect that we have adopted a new corporate form called a listed stock corporation (*sociedad anónima bursátil*, or the initials *S.A.B.*);

redefinition of the functions and structure of the Board of Directors, whereby, among others, the management of the company is entrusted to the board of directors and also to the company's chief executive officer, who is required to follow the strategies, policies and guidelines approved by the board of directors and the authority, obligations and duties expressly authorized in the Mexican Securities Law;

surveillance is entrusted to the Board of Directors, which is assisted by the Corporate Practices Committee that has been recently created for such purposes, the Audit Committee and our external auditor;

the Corporate Practices Committee and the Audit Committee consist solely of independent directors, each committee is formed by at least 3 board members appointed by the shareholders or by the board of directors, as proposed by the chairman of the board of directors;

the chairmen of the Corporate Practices Committee and the Audit Committee are appointed (taking into consideration their experience, capacity and professional prestige) and removed exclusively by a shareholders' meeting, provided that the chairmen shall not also serve as chairman of the board of directors;

elimination of the role and responsibilities of the statutory examiner (*comisario*), whose responsibilities have been assumed by the board of directors through the new Corporate Practices Committee and the Audit Committee, as well as by our external auditor;

ability to have the external auditor attend meetings of the board of directors, as an observer with a right to participate, but without voting rights;

the ability to call a meeting of the board of directors, and to cause items to be added to the agenda, is now extended to the chairman of the board of directors, the chairman of the new Corporate Practices Committee and the Audit Committee, or to at least 25% of the members of the board of directors;

independence of members of the board of directors is now determined through a shareholders' meeting, subject to CNBV's authority to challenge such determination;

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directors may continue in the exercise of their functions even if the term for which they have been appointed has concluded, up to a term of 30 calendar days; the board of directors is entitled to appoint interim members, without need of a shareholders meeting, in the event of an absence of any member of

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the board of directors, or if the appointed members does not accept or take office and no alternate director was appointed or such alternate did not take office;

holders of Series D and L Shares are entitled to vote in the matters expressly set forth in the Mexican Securities Law; and

any capital increase by means of an issuance of non-subscribed shares to be held in treasury of the company requires approval at an extraordinary shareholders meeting.

### ***Organization and Register***

We are a *sociedad anónima bursátil de capital variable* organized in Mexico under the Mexican General Corporations Law. We were incorporated in 1936 under the name Valores Industriales, S.A., as a *sociedad anónima*, and are currently named Fomento Económico Mexicano, S.A.B. de C.V. On December 5, 2006, as required by the new Mexican Securities Law, we changed our name to reflect that we are a *sociedad anónima bursátil de capital variable* (a variable capital listed stock corporation), whereas previously companies names in Mexico, including ours, did not indicate whether the company was a listed company (*sociedad anónima de capital variable*). We were registered in the Public Registry of Commerce of Monterrey, Nuevo León on May 30, 1936 under the mercantile number 16, page 168, volume 79, third book, second auxiliary of the Registry.

### ***Voting Rights and Certain Minority Rights***

Each Series B Share entitles its holder to one vote at any of our ordinary or extraordinary general shareholders meetings. Our bylaws state that the board of directors must comprise no more than 21 members. Holders of Series B Shares are entitled to elect at least 11 members of our board of directors. Holders of Series D-B and D-L Shares are entitled to elect five members of our board of directors and, upon conversion of the Series D-L Shares to Series L Shares or upon issuance of Series L Shares, the holders of Series L Shares will be entitled to elect two members of the board of directors. None of our shares has cumulative voting rights, which are not customary for Mexican companies.

Under our bylaws, the holders of Series D and L Shares are entitled to vote at extraordinary shareholders meetings called to consider any of the following limited matters: (1) the transformation from one form of corporate organization to another, other than from a company with variable capital stock to a company without variable capital stock or vice versa, (2) any merger in which we are not the surviving entity or with other entities whose principal corporate purposes are different from those of our company or our subsidiaries, (3) change of nationality, (4) dissolution and liquidation and (5) the cancellation of the registration of the Series D Shares or Series L Shares in the Mexican Stock Exchange or in any other foreign stock market where listed, except in the case of the conversion of these shares as provided for in our bylaws.

Under Mexican law, holders of shares of any series are entitled to vote as a class in a special meeting governed by the same rules that apply to extraordinary shareholders meetings on any action that would have an effect on the rights of holders of shares of such series. There are no procedures for determining whether a particular proposed shareholder action requires a class vote, and Mexican law does not provide extensive guidance on the criteria to be applied in making such a determination.

Pursuant to the Mexican Securities Market Law and the Mexican General Corporations Law, our bylaws include a number of minority shareholder protections. These minority protections include provisions that permit:

holders of at least 10% of our outstanding capital stock entitled to vote (including in a limited or restricted manner) may require the chairman of the board of directors or of the Audit Committee or Corporate Practices Committee to call a shareholders meeting;

holders of at least 5% of our outstanding capital stock may bring an action for liabilities against our directors, the secretary of the board of directors or the relevant officers;

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holders of at least 10% of our outstanding capital stock who are entitled to vote, including limited or restricted vote, at any shareholders meeting to request that resolutions with respect to any matter on which they considered they were not sufficiently informed be postponed;

holders of 20% of our outstanding capital stock to oppose any resolution adopted at a shareholders meeting in which they are entitled to vote, including limited or restricted vote, and file a petition for a court order to suspend the resolution temporarily within 15 days following the adjournment of the meeting at which the action was taken, provided that (1) the challenged resolution violates Mexican law or our bylaws, (2) the opposing shareholders neither attended the meeting nor voted in favor of the challenged resolution and (3) the opposing shareholders deliver a bond to the court to secure payment of any damages that we may suffer as a result of suspending the resolution in the event that the court ultimately rules against the opposing shareholder; and

holders of at least 10% of our outstanding capital stock who are entitled to vote, including limited or restricted vote, to appoint one member of our board of directors and one alternate member of our board of directors.

## **Shareholders Meetings**

General shareholders meetings may be ordinary meetings or extraordinary meetings. Extraordinary meetings are those called to consider certain matters specified in Article 182 and 228 bis. of the Mexican General Corporations Law, Article 53 of the Mexican Securities Law and in our bylaws. These matters include: amendments to our bylaws, liquidation, dissolution, merger and transformation from one form of corporate organization to another, issuance of preferred stock and increases and reductions of the fixed portion of our capital stock. In addition, our bylaws require an extraordinary meeting to consider the cancellation of the registration of shares with the Mexican Registry of Securities, or RNV or with other foreign stock exchanges on which our shares may be listed, the amortization of distributable earnings into capital stock and an increase in our capital stock in terms of the Mexican Securities Law. General meetings called to consider all other matters, including increases or decreases affecting the variable portion of our capital stock, are ordinary meetings. An ordinary meeting must be held at least once each year within the first four months following the end of the preceding fiscal year. Holders of BD Units or B Units, and beginning on May 11, 2008, holders of B Shares, are entitled to attend all shareholders meetings of the Series B Shares and Series D Shares included in the BD Units or B Units and to vote on matters that are subject to the vote of holders of the underlying shares.

The quorum for an ordinary shareholders meeting of the Series B Shares on first call is more than 50% of the Series B Shares, and action may be taken by a majority of the Series B Shares represented at the meeting. If a quorum is not available, a second or subsequent meeting may be called and held by whatever number of Series B Shares is represented at the meeting, at which meeting action may be taken by a majority of the Series B Shares that are represented at the meeting.

The quorum for an extraordinary shareholders meeting is at least 75% of the shares entitled to vote at the meeting, and action may be taken by a vote of the majority of all the outstanding shares that are entitled to vote. If a quorum is not available, a second meeting may be called, at which the quorum will be the majority of the outstanding capital stock entitled to vote, and actions will be taken by holders of the majority of all the outstanding capital stock entitled to vote.

Shareholders meetings may be called by the board of directors, the Audit Committee or the Corporate Practice Committee and, under certain circumstances, a Mexican court. Holders of 10% or more of our capital stock may require the chairman of the board of directors, or the chairman of the Audit Committee or Corporate Practices Committee to call a shareholders meeting. A notice of meeting and an agenda must be published in the *Periódico Oficial del Estado de Nuevo León* (the Official State Gazette of Nuevo León) or a newspaper of general circulation in Monterrey, Nuevo León, Mexico at least 15 days prior to the date set for the meeting. Notices must set forth the place, date and time of the meeting and the matters to be addressed and must be signed by whomever convened the meeting. Shareholders meetings will be deemed validly held and convened without a prior notice or

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publication whenever all the shares representing our capital stock are fully represented. All relevant information relating to the shareholders meeting must be made available to shareholders starting on the date of publication of the notice. To attend a meeting, shareholders must deposit their shares with the company or with Indeval or an institution for the deposit of securities prior to the meeting as indicated in the notice. If entitled to attend a meeting, a shareholder may be represented by an attorney-in-fact.

### ***Dividend Rights***

At the annual ordinary general shareholders meeting, the board of directors submits the financial statements of the company for the previous fiscal year, together with a report thereon by the board of directors. Once the holders of Series B Shares have approved the financial statements, they determine the allocation of our net profits for the preceding year. Mexican law requires the allocation of at least 5% of net profits to a legal reserve, which is not subsequently available for distribution, until the amount of the legal reserve equals 20% of our paid in capital stock. Thereafter, the holders of Series B Shares may determine and allocate a certain percentage of net profits to any general or special reserve, including a reserve for open-market purchases of our shares. The remainder of net profits is available for distribution in the form of dividends to the shareholders. Dividends may only be paid if net profits are sufficient to offset losses from prior fiscal years.

Amounts allocated as dividends will be paid to the holders of capital stock of our company in the following manner. Our bylaws provide that, before May 11, 2008, dividends will be allocated among the shares outstanding and fully paid at the time a dividend is declared in such manner that each Series D-B Share and Series D-L Share receives 125% of the dividend distributed in respect of each Series B Share. Holders of Series D-B Shares and Series D-L Shares are entitled to this dividend premium in connection with all dividends paid by us. On May 11, 2008, the Series D-B Shares will automatically convert into Series B Shares and the Series D-L Shares will automatically convert into Series L Shares, which will not be entitled to a dividend premium. From and after May 11, 2008, the Series B Shares and Series L Shares that are outstanding and fully paid at the time a dividend is declared will be entitled to share equally in any dividend.

### ***Change in Capital and Withdrawal Rights***

Our outstanding capital stock consists of both a fixed and a variable portion. The fixed portion of our capital stock may be increased or decreased only by an amendment of the bylaws adopted by an extraordinary shareholders meeting. The variable portion of our capital stock may be increased or decreased by resolution of an ordinary shareholders meeting. Capital increases and decreases must be recorded in our share registry and book of capital variations, if applicable.

A capital stock increase may be effected through the issuance of new shares for payment in cash or in kind, or by capitalization of indebtedness or of certain items of stockholders' equity. Treasury stock may only be sold pursuant to a public offering.

Any increase or decrease in our capital stock or any redemption or repurchase will be subject to the following limitations: (1) Series B Shares will always represent at least 51% of our outstanding capital stock and the Series D-L Shares and Series L Shares will never represent more than 25% of our outstanding capital stock; (2) before May 11, 2008, the Series D-B, Series D-L and Series L Shares will not exceed, in the aggregate, 49% of our outstanding capital stock; and (3) from and after May 11, 2008, no Series D Shares will be outstanding, the Series L Shares will represent up to 25% of our outstanding capital stock and the Series B Shares will represent at least 75% of our outstanding capital stock.

### ***Preemptive Rights***

Under Mexican law, except in limited circumstances which are described below, in the event of an increase in our capital stock, a holder of record generally has the right to subscribe to shares of a series held by such holder sufficient to maintain such holder's existing proportionate holding of shares of that series. Preemptive rights must be exercised during a term fixed by the shareholders at the meeting declaring the capital increase, which term



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must last at least 15 days following the publication of notice of the capital increase in the Official State Gazette. As a result of applicable United States securities laws, holders of ADSs may be restricted in their ability to participate in the exercise of preemptive rights under the terms of the deposit agreement. Shares subject to a preemptive rights offering, with respect to which preemptive rights have not been exercised, may be sold by us to third parties on the same terms and conditions previously approved by the shareholders or the board of directors. Under Mexican law, preemptive rights cannot be waived in advance or be assigned, or be represented by an instrument that is negotiable separately from the corresponding shares.

Our bylaws provide that shareholders will not have preemptive rights to subscribe shares in the event of a capital stock increase in the following events: (1) merger of the Company; (2) conversion of obligations in terms of the Mexican General Corporations Law; (3) public offering in terms of articles 53 and 56 of the Mexican Securities Law; (4) capital increase made through the payment in kind of the issued shares or through the cancellation of debt of the Company; and (5) issuance of shares acquired by the company.

### ***Limitations on Share Ownership***

Ownership by non-Mexican nationals of shares of Mexican companies is regulated by the Foreign Investment Law and its regulations. The Foreign Investment Commission is responsible for the administration of the Foreign Investment Law and its regulations.

As a general rule, the Foreign Investment Law allows foreign holdings of up to 100% of the capital stock of Mexican companies, except for those companies engaged in certain specified restricted industries. The Foreign Investment Law and its regulations require that Mexican shareholders retain the power to determine the administrative control and the management of corporations in industries in which special restrictions on foreign holdings are applicable. Foreign investment in our shares is not limited under either the Foreign Investment Law or its regulations.

### ***Authority of the Board of Directors***

The board of directors is our legal representative and is authorized to take any action in connection with our operations not expressly reserved to our shareholders. Pursuant to the Mexican Securities Law, the board of directors must approve, observing at all moments their duty of care and duty of loyalty, among other matters:

any transactions with related parties outside the ordinary course of our business

significant asset transfers or acquisitions;

material guarantees or collateral;

internal policies; and

other material transactions.

Meetings of the board of directors are validly convened and held if a majority of the members are present. Resolutions passed at these meetings will be valid if approved by a majority of members of the board of directors are present at the meeting. If required, the chairman of the board of directors may cast a tie-breaking vote.

### ***Redemption***

We may redeem part of our shares for cancellation with distributable earnings pursuant to a decision of an extraordinary shareholders meeting. Only shares subscribed and fully paid for may be redeemed. Any shares intended to be redeemed shall be purchased on the Mexican Stock Exchange in accordance with the Mexican General Corporations Law and the Mexican Securities Market Law. No shares will be redeemed, if as a consequence of such redemption, the Series D and Series L Shares in the aggregate exceed the percentages permitted by our bylaws or if any

such redemption will reduce our fixed capital below its minimum.

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### ***Repurchase of Shares***

According to our bylaws, subject to the provisions of the Mexican Securities Law and under rules promulgated by the CNBV, we may repurchase our shares.

In accordance with the Mexican Securities Law, our subsidiaries may not purchase, directly or indirectly, shares of our capital stock or any security that represents such shares.

### ***Forfeiture of Shares***

As required by Mexican law, our bylaws provide that non-Mexican holders of BD Units, B Units or shares (1) are considered to be Mexican with respect to such shares that they acquire or hold and (2) may not invoke the protection of their own governments in respect of the investment represented by those shares. Failure to comply with our bylaws may result in a penalty of forfeiture of a shareholder's capital stock in favor of the Mexican state. In the opinion of Lic. Carlos Aldrete Ancira, our general counsel, under this provision, a non-Mexican shareholder (including a non-Mexican holder of ADSs) is deemed to have agreed not to invoke the protection of its own government by asking such government to interpose a diplomatic claim against the Mexican state with respect to its rights as a shareholder, but is not deemed to have waived any other rights it may have, including any rights under the United States securities laws, with respect to its investment in our company. If a shareholder should invoke governmental protection in violation of this agreement, its shares could be forfeited to the Mexican state.

### ***Duration***

The bylaws provide that the duration of our company is 99 years, commencing on May 30, 1936.

### ***Appraisal Rights***

Whenever the shareholders approve a change of corporate purpose, change of nationality or the transformation from one form of corporate organization to another, any shareholder entitled to vote on such change that has voted against it, may withdraw as a shareholder of our company and have its shares redeemed by FEMSA at a price per share calculated as specified under applicable Mexican law, provided that it exercises its right within 15 days following the adjournment of the meeting at which the change was approved. Under Mexican law, the amount which a withdrawing shareholder is entitled to receive is equal to its proportionate interest in our capital stock or according to our most recent balance sheet approved by an ordinary general shareholders meeting.

### ***Delisting of Shares***

In the event of a cancellation of the registration of any of our shares with the RNV, whether by order of the CNBV or at our request with the prior consent of 95% of the holders of our outstanding capital stock, our bylaws and the new Mexican Securities Law require us to make a public offer to acquire these shares prior to their cancellation.

### ***Liquidation***

Upon the dissolution of our company, one or more liquidators must be appointed by an extraordinary general meeting of the shareholders to wind up its affairs. All fully paid and outstanding shares of capital stock will be entitled to participate equally in any distribution upon liquidation.

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### ***Actions Against Directors***

Shareholders (including holders of Series D-B and Series D-L Shares) representing, in the aggregate, not less than 5% of our capital stock may directly bring an action against directors.

In the event of actions derived from any breach of the duty of care and the duty of loyalty, liability is exclusively in favor of the company. The Mexican Securities Law, contrary to the previous securities law, establishes that liability may be imposed on the members and the secretary of the board of directors, as well as to the relevant officers.

Notwithstanding, the Mexican Securities Law provides that the members of the board of directors will not incur, individually or jointly, liability for damages and losses caused to the company, when their acts were made in good faith, in any of the following events (1) the directors complied with the requirements of the Mexican Securities Law and with the company's bylaws, (2) the decision making or voting was based on information provided by the relevant officers, the external auditor or the independent experts, whose capacity and credibility do not offer reasonable doubt; (3) the negative economic effects could not have been foreseen, based on the information available; and (4) they comply with the resolutions of the shareholders' meeting when such resolutions comply with applicable law.

### ***Fiduciary Duties Duty of Care***

The Mexican Securities Law provides that the directors shall act in good faith and in our best interest and in the best interest of our subsidiaries. In order to fulfill its duty, the board of directors may:

request information about us or our subsidiaries that is reasonably necessary to fulfill its duties;

require our officers and certain other persons, including the external auditors, to appear at board of directors' meetings to report to the board of directors;

postpone board of directors' meetings for up to three days when a director has not been given sufficient notice of the meeting or in the event that a director has not been provided with the information provided to the other directors; and

require a matter be discussed and voted upon by the full board of directors in the presence of the secretary of the board of directors. Our directors may be liable for damages for failing to comply their duty of care if such failure causes economic damage to us or our subsidiaries and the director (1) failed to attend, board of directors' or committee meetings and as a result of, such failure, the board of directors was unable to take action, unless such absence is approved by the shareholders meeting, (2) failed to disclose to the board of directors or the committees material information necessary for the board of directors to reach a decision, unless legally or contractually prohibited from doing so in order to maintain confidentiality, and (3) failed to comply with the duties imposed by the Mexican Securities Law or our bylaws.

### ***Fiduciary Duties Duty of Loyalty***

The Mexican Securities Law provides that the directors and secretary of the board of directors shall keep confidential any non-public information and matters about which they have knowledge as a result of their position. Also, directors should abstain from participating, attending or voting at meetings related to matters where they have a conflict of interest.

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The directors and secretary of the board of directors will be deemed to have violated the duty of loyalty, and will be liable for damages, when they obtain an economic benefit by virtue of their position. Further, the directors will fail to comply with their duty of loyalty if they:

vote at a board of directors meeting or take any action on a matter involving our assets where there is a conflict of interest;

fail to disclose a conflict of interest during a board of directors meeting;

enter into a voting arrangement to support a particular shareholder or group of shareholders against the other shareholders;

approve of transactions without complying with the requirements of the Mexican Securities Law;

use company property in violation of the policies approved by the board of directors;

unlawfully use material non-public information; and

usurp a corporate opportunity for their own benefit or the benefit of third parties, without the prior approval of the board of directors.

### ***Limited Liability***

The liability of shareholders for our company's losses is limited to their shareholdings in our company.

### **Taxation**

The following summary contains a description of certain U.S. federal income and Mexican federal tax consequences of the purchase, ownership and disposition of our ADSs by a holder that is a citizen or resident of the United States, a U.S. domestic corporation or a person or entity that otherwise will be subject to U.S. federal income tax on a net income basis in respect of our ADSs, whom we refer to as a U.S. holder, but it does not purport to be a description of all of the possible tax considerations that may be relevant to a decision to purchase, hold or dispose of ADSs. In particular, this discussion does not address all Mexican or U.S. federal income tax considerations that may be relevant to a particular investor, nor does it address the special tax rules applicable to certain categories of investors, such as banks, dealers, traders who elect to mark to market, tax-exempt entities, insurance companies, certain short-term holders of ADSs or investors who hold our ADSs as part of a hedge, straddle, conversion or integrated transaction or investors who have a functional currency other than the U.S. dollar. This summary deals only with U.S. holders that will hold our ADSs as capital assets and does not address the tax treatment of a U.S. holder that owns or is treated as owning 10% or more of the voting shares (including ADSs) of the company.

This summary is based upon the federal tax laws of the United States and Mexico as in effect on the date of this annual report, including the provisions of the income tax treaty between the United States and Mexico which we refer to as the Tax Treaty, which are subject to change. The summary does not address any tax consequences under the laws of any state or locality of Mexico or the United States or the laws of any taxing jurisdiction other than the federal laws of Mexico and the United States. Holders of our ADSs should consult their tax advisors as to the U.S., Mexican or other tax consequences of the purchase, ownership and disposition of ADSs, including, in particular, the effect of any foreign, state or local tax laws.

### ***Mexican Taxation***

For purposes of this summary, the term non-resident holder means a holder that is not a resident of Mexico for tax purposes and that does not hold our ADSs in connection with the conduct of a trade or business through a permanent establishment for tax purposes in Mexico. For purposes of Mexican taxation, an individual is



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a resident of Mexico if he or she has established his or her home in Mexico, or if he or she has another home outside Mexico, but his or her Centro de Intereses Vitales (Center of Vital Interests) (as defined in the Mexican Tax Code) is located in Mexico. A legal entity is a resident of Mexico either if it has its principal place of business or its place of effective management in Mexico. A Mexican citizen is presumed to be a resident of Mexico unless he or she can demonstrate that the contrary is true. If a legal entity or an individual is deemed to have a permanent establishment in Mexico for tax purposes, all income attributable to the permanent establishment will be subject to Mexican taxes, in accordance with applicable tax laws.

*Taxation of Dividends.* Under Mexican income tax law, dividends, either in cash or in kind, paid with respect to our shares represented by our ADSs are not subject to Mexican withholding tax.

*Taxation of Dispositions of ADSs.* Gains from the sale or disposition of ADSs by non-resident holders will not be subject to Mexican tax, if the disposition is carried out through a stock exchange recognized under applicable Mexican tax law.

Gains on the sale or other disposition of ADSs made in circumstances different from those set forth in the prior paragraph generally would be subject to Mexican tax, regardless of the nationality or residence of the transferor. However, under the Tax Treaty, a holder that is eligible to claim the benefits of the Tax Treaty will be exempt from Mexican tax on gains realized on a sale or other disposition of our ADSs in a transaction that is not carried out through the Mexican Stock Exchange or other approved securities markets, so long as the holder did not own, directly or indirectly, 25% or more of our outstanding capital stock (including shares represented by our ADSs) within the 12-month period preceding such sale or other disposition. Deposits of shares in exchange for ADSs and withdrawals of shares in exchange for our ADSs will not give rise to Mexican tax.

*Other Mexican Taxes.* There are no Mexican inheritance, gift, succession or value added taxes applicable to the ownership, transfer, exchange or disposition of our ADSs. There are no Mexican stamp, issue, registration or similar taxes or duties payable by holders of our ADSs.

***United States Taxation***

*Taxation of Dividends.* The gross amount of any dividends paid with respect to our shares represented by our ADSs generally will be included in the gross income of a U.S. holder as ordinary income on the day on which the dividends are received by the ADS depository and will not be eligible for the dividends received deduction allowed to corporations under the Internal Revenue Code of 1986, as amended. Dividends, which will be paid in Mexican pesos, will be includible in the income of a U.S. holder in a U.S. dollar amount calculated, in general, by reference to the exchange rate in effect on the date that they are received by the ADS depository (regardless of whether such Mexican pesos are in fact converted into U.S. dollars on such date). If such dividends are converted into U.S. dollars on the date of receipt, a U.S. holder generally should not be required to recognize foreign currency gain or loss in respect of the dividends. U.S. holders should consult their tax advisors regarding the treatment of the foreign currency gain or loss, if any, on any Mexican pesos received that are converted into U.S. dollars on a date subsequent to the date of receipt. Subject to certain exceptions for short-term and hedged positions, the U.S. dollar amount of dividends received by an individual U.S. holder in respect of the ADSs for taxable years beginning before January 1, 2011 is subject to taxation at a maximum rate of 15% if the dividends are qualified dividends. Dividends paid on the ADSs will be treated as qualified dividends if (1) we are eligible for the benefits of a comprehensive income tax treaty with the United States that the Internal Revenue Service has approved for the purposes of the qualified dividend rules and (2) we were not, in the year prior to the year in which the dividend was paid, and are not, in the year in which the dividend is paid, a passive foreign investment company. The income tax treaty between Mexico and the United States has been approved for the purposes of the qualified dividend rules. Based on our audited consolidated financial statements and relevant market and shareholder data, we believe that we were not treated as a passive foreign investment company for U.S. federal income tax purposes with respect to our 2006 taxable year. In addition, based on our audited consolidated financial statements and our current expectations regarding the value and nature of our assets, the sources and nature of our income, and relevant market and shareholder data, we do not anticipate becoming a passive foreign investment company for our 2007 taxable year. Dividends generally will constitute foreign source passive income for U.S. foreign tax credit purposes.

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Distributions to holders of additional shares with respect to our ADSs that are made as part of a pro rata distribution to all of our shareholders generally will not be subject to U.S. federal income tax.

A holder of ADSs that is, with respect to the United States, a foreign corporation or non-U.S. holder generally will not be subject to U.S. federal income or withholding tax on dividends received on ADSs unless such income is effectively connected with the conduct by the non-U.S. holder of a trade or business in the United States.

*Taxation of Capital Gains.* A gain or loss realized by a U.S. holder on the sale or other disposition of ADSs will be subject to U.S. federal income taxation as a capital gain or loss in an amount equal to the difference between the amount realized on the disposition and such U.S. holder's tax basis in the ADSs. Any such gain or loss will be a long-term capital gain or loss if the ADSs were held for more than one year on the date of such sale. Any long-term capital gain recognized by a U.S. holder that is an individual is subject to a reduced rate of federal income taxation. The deduction of capital losses is subject to limitations for U.S. federal income tax purposes. Deposits and withdrawals of shares by U.S. holders in exchange for ADSs will not result in the realization of gains or losses for U.S. federal income tax purposes.

Any gain realized by a U.S. holder on the sale or other disposition of ADSs will be treated as U.S. source income for U.S. foreign tax credit purposes.

A non-U.S. holder of ADSs will not be subject to U.S. federal income or withholding tax on any gain realized on the sale of ADSs, unless (1) such gain is effectively connected with the conduct by the non-U.S. holder of a trade or business in the United States, or (2) in the case of a gain realized by an individual non-U.S. holder, the non-U.S. holder is present in the United States for 183 days or more in the taxable year of the sale and certain other conditions are met.

*United States Backup Withholding and Information Reporting.* A U.S. holder of ADSs may, under certain circumstances, be subject to backup withholding with respect to certain payments to such U.S. holder, such as dividends, interest or the proceeds of a sale or disposition of ADSs, unless such holder (1) is a corporation or comes within certain exempt categories, and demonstrates this fact when so required, or (2) provides a correct taxpayer identification number, certifies that it is not subject to backup withholding and otherwise complies with applicable requirements of the backup withholding rules. Any amount withheld under these rules does not constitute a separate tax and will be creditable against the holder's U.S. federal income tax liability. While non-U.S. holders generally are exempt from backup withholding, a non-U.S. holder may, in certain circumstances, be required to comply with certain information and identification procedures in order to prove this exemption.

## **Material Contracts**

We and our subsidiaries are parties to a variety of material agreements with third parties, including shareholders' agreements, supply agreements and purchase and service agreements. Set forth below are summaries of the material terms of such agreements. The actual agreements have either been filed as exhibits to, or incorporated by reference in, this annual report. See Item 19. Exhibits.

## **Coca-Cola FEMSA**

### ***Shareholders Agreement***

Coca-Cola FEMSA operates pursuant to a shareholders agreement among two subsidiaries of FEMSA, The Coca-Cola Company and certain of its subsidiaries. This agreement, together with Coca-Cola FEMSA's bylaws, sets forth the basic rules under which Coca-Cola FEMSA operates.

The shareholders agreement contemplates that Coca-Cola FEMSA will be managed in accordance with one-year and five-year business plans, although in practice, it is now managed according to a three-year plan.

Under Coca-Cola FEMSA's bylaws, its Series A Shares and Series D Shares are the only shares with full voting rights and, therefore, control actions by its shareholders and board of directors. The holders of Series A Shares and Series D Shares have the power to determine the outcome of all actions requiring approval by its board.



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of directors and, except in certain limited situations, all actions requiring approval of the shareholders. For actions by its board of directors, a supermajority including the directors appointed by the holders of Series D Shares is required.

The shareholders agreement sets forth the principal shareholders' understanding as to the effect of adverse actions of The Coca-Cola Company under the bottler agreements. Coca-Cola FEMSA's bylaws provide that a majority of the directors appointed by the holders of Series A Shares, upon making a reasonable, good faith determination that any action of The Coca-Cola Company under any bottler agreement between The Coca-Cola Company and Coca-Cola FEMSA or any of its subsidiaries is materially adverse to Coca-Cola FEMSA's business interests and that The Coca-Cola Company has failed to cure such action within 60 days of notice, may declare a simple majority period at any time within 90 days after giving notice. During the simple majority period certain decisions, namely the approval of material changes in Coca-Cola FEMSA's business plans, the introduction of a new, or termination of an existing, line of business, and related party transactions outside the ordinary course of business, which would ordinarily require the presence and approval of at least two Series D directors, can be made by a simple majority vote of its entire board of directors, without requiring the presence or approval of any Series D director. A majority of the Series A directors may terminate a simple majority period but, once having done so, cannot declare another simple majority period for one year after the termination. If a simple majority period persists for one year or more, the provisions of the shareholders agreement for resolution of irreconcilable differences may be triggered, with the consequences outlined in the following paragraph.

In addition to the rights of first refusal provided for in Coca-Cola FEMSA's bylaws regarding proposed transfers of Series A Shares or Series D Shares, the shareholders agreement contemplates three circumstances under which one principal shareholder may purchase the interest of the other in Coca-Cola FEMSA: (1) a change in control in a principal shareholder; (2) the existence of irreconcilable differences between the principal shareholders; or (3) the occurrence of certain specified defaults.

In the event that (1) one of the principal shareholders buys the other's interest in Coca-Cola FEMSA in any of the circumstances described above or (2) the ownership of Coca-Cola FEMSA's shares of capital stock other than the Series L Shares of the subsidiaries of The Coca-Cola Company or FEMSA is reduced below 20% and upon the request of the shareholder whose interest is not so reduced, the shareholders agreement requires that Coca-Cola FEMSA's bylaws be amended to eliminate all share transfer restrictions and all super-majority voting and quorum requirements, after which the shareholders agreement would terminate. In the event that the ownership of Coca-Cola FEMSA's shares of capital stock other than the Series L Shares of the subsidiaries of The Coca-Cola Company or FEMSA is reduced below 25% (but not below 20%) and upon the request of the shareholder whose interest is not so reduced, the shareholders agreement requires that Coca-Cola FEMSA's bylaws be amended to eliminate all super-majority voting and quorum requirements, other than those relating to the share transfer restrictions.

The shareholders agreement also contains provisions relating to the principal shareholders' understanding as to Coca-Cola FEMSA's growth. It states that it is The Coca-Cola Company's intention that Coca-Cola FEMSA will be viewed as one of a small number of its anchor bottlers in Latin America. In particular, the parties agree that it is desirable that Coca-Cola FEMSA expands by acquiring additional bottler territories in Mexico and other Latin American countries in the event any become available through horizontal growth. In addition, The Coca-Cola Company has agreed, subject to a number of conditions, that if it obtains ownership of a bottler territory that fits with Coca-Cola FEMSA's operations, it will give Coca-Cola FEMSA the option to acquire such territory. The Coca-Cola Company has also agreed to support prudent and sound modifications to Coca-Cola FEMSA's capital structure to support horizontal growth. The Coca-Cola Company's agreement as to horizontal growth expires upon either the elimination of the super-majority voting requirements described above or The Coca-Cola Company's election to terminate the agreement as a result of a default.

***The Coca-Cola Memorandum***

In connection with the acquisition of Panamco, Coca-Cola FEMSA established certain understandings primarily relating to operational and business issues with both The Coca-Cola Company and our company that were memorialized in writing prior to completion of the acquisition. The terms are as follows:

The current stockholder arrangements between our company and The Coca-Cola Company will continue in place. See Shareholders Agreement.

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We will continue to consolidate Coca-Cola FEMSA's financial results.

The Coca-Cola Company and our company will continue to discuss in good faith the possibility of implementing changes to Coca-Cola FEMSA's capital structure in the future.

There will be no changes in concentrate incidence pricing or marketing support by The Coca-Cola Company up to May 2004. After such time, The Coca-Cola Company has complete discretion to implement any changes with respect to these matters, but any decision in this regard will be discussed with Coca-Cola FEMSA and will take Coca-Cola FEMSA's operating condition into consideration.

The Coca-Cola Company may require the establishment of a different long-term strategy for Brazil. If, after taking into account Coca-Cola FEMSA's performance in Brazil, The Coca-Cola Company does not consider Coca-Cola FEMSA to be part of this long-term strategic solution for Brazil, then Coca-Cola FEMSA will sell its Brazilian franchise to The Coca-Cola Company or its designee at fair market value. Fair market value would be determined by independent investment bankers retained by each party at their own expense pursuant to specified procedures.

FEMSA, The Coca-Cola Company and Coca-Cola FEMSA will meet to discuss the optimal Latin American territorial configuration for the Coca-Cola bottler system. During this meeting, Coca-Cola FEMSA will consider all possible combinations and any asset swap transactions that may arise from these discussions. In addition, Coca-Cola FEMSA will entertain any potential combination as long as it is strategically sound and done at fair market value.

Coca-Cola FEMSA would like to keep open strategic alternatives that relate to the integration of carbonated soft drinks and beer. The Coca-Cola Company, our company and Coca-Cola FEMSA would explore these alternatives on a market-by-market basis at the appropriate time.

The Coca-Cola Company agreed to sell to a subsidiary of our company sufficient shares to permit FEMSA to beneficially own 51% of Coca-Cola FEMSA's outstanding capital stock (assuming that this subsidiary of FEMSA does not sell any shares and that there are no issuances of Coca-Cola FEMSA's stock other than as contemplated by the acquisition). As a result of this understanding, on November 3, 2006, FEMSA acquired, through its subsidiary CIBSA, 148,000,000 of Coca-Cola FEMSA's Series D Shares from certain subsidiaries of The Coca-Cola Company, representing 9.4% of the total outstanding voting shares and 8.02% of the total outstanding equity of Coca-Cola FEMSA, at a price of US\$ 2.888 per share for an aggregate amount of US\$ 427.4 million. Pursuant to Coca-Cola FEMSA's bylaws, the acquired shares were converted from Series D Shares to Series A Shares.

Coca-Cola FEMSA may be entering some markets where significant infrastructure investment may be required. The Coca-Cola Company and FEMSA will conduct a joint study that will outline strategies for these markets, as well as the investment levels required to execute these strategies. Subsequently, it is intended that our company and The Coca-Cola Company will reach agreement on the level of funding to be provided by each of the partners. The parties intend that this allocation of funding responsibilities would not be overly burdensome for either partner.

Coca-Cola FEMSA entered into a stand-by credit facility, on December 19, 2003 with The Coca-Cola Export Corporation, which expired in December 2006.

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### ***New Cooperation Framework with the Coca-Cola Company***

On September 1, 2006, Coca-Cola FEMSA and The Coca-Cola Company arrived at a comprehensive cooperation framework for a new stage of collaboration going forward. This new framework includes the main aspects of Coca-Cola FEMSA's relationship with The Coca-Cola Company and defines the terms for the new collaborative business model. The framework is structured around three main objectives:

*Sustainable growth of carbonated soft drinks and non-carbonated beverages:* Together with The Coca-Cola Company, Coca-Cola FEMSA has defined a platform to jointly pursue, organically and through acquisitions, incremental growth in the carbonated soft drink category, as well as accelerated development in the non-carbonated segment across Latin America. To this end, The Coca-Cola Company will provide a relevant portion of the funds derived from the incidence increase to marketing support of the carbonated and non-carbonated soft drinks portfolio. In addition, the new framework contemplates a new, all-encompassing business model for the development of the non-carbonated segment that further aligns Coca-Cola FEMSA's and The Coca-Cola Company's objectives and should contribute to incremental long-term value creation at both companies.

*Horizontal growth:* The new framework includes The Coca-Cola Company's endorsement of Coca-Cola FEMSA's aspiration to continue being a leading participant in the consolidation of the Coca-Cola system in Latin America, as well as the exploration of potential opportunities in other markets where Coca-Cola FEMSA's operating model and strong execution capabilities could be leveraged.

*Long-term vision in relationship economics:* Coca-Cola FEMSA and The Coca-Cola Company understand each other's business objectives and growth plans, and the new framework provides long-term perspective on the economics of their relationship. This will allow Coca-Cola FEMSA and The Coca-Cola Company to focus on continuing to drive the business forward and generating profitable growth.

### ***Bottler Agreements***

Bottler agreements are the standard agreements that The Coca-Cola Company enters into with bottlers outside the United States for the sale of concentrates for certain Coca-Cola trademark beverages. Coca-Cola FEMSA manufactures, packages, distributes and sells soft drink beverages and bottled water under a separate bottler agreement for each of its territories.

These bottler agreements provide that Coca-Cola FEMSA will purchase its entire requirement of concentrates for *Coca-Cola* trademark beverages from The Coca-Cola Company and other authorized suppliers at prices, terms of payment and on other terms and conditions of supply as determined from time to time by The Coca-Cola Company at its sole discretion. Concentrate prices are determined as a percentage of the weighted average retail price in local currency, net of applicable taxes. Although the price multipliers used to calculate the cost of concentrate and the currency of payment, among other terms, are set by The Coca-Cola Company at its sole discretion, Coca-Cola FEMSA sets the price of products sold to retailers at its discretion, subject to the applicability of price restraints. Coca-Cola FEMSA has the exclusive right to distribute Coca-Cola trademark beverages for sale in its territories in authorized containers of the nature prescribed by the bottler agreements and currently used by Coca-Cola FEMSA. These containers include various configurations of cans and returnable and non-returnable bottles made of glass and plastic and fountain containers.

The bottler agreements include an acknowledgment by Coca-Cola FEMSA that The Coca-Cola Company is the sole owner of the trademarks that identify the Coca-Cola trademark beverages and of the secret formulas with which The Coca-Cola Company's concentrates are made. Subject to Coca-Cola FEMSA's exclusive right to distribute Coca-Cola trademark beverages in its territories, The Coca-Cola Company reserves the right to import and export Coca-Cola trademark beverages to and from each of its territories. Coca-Cola FEMSA's bottler agreements do not contain restrictions on The Coca-Cola Company's ability to set the price of concentrates charged to its subsidiaries and do not impose minimum marketing obligations on The Coca-Cola Company. The prices at which Coca-Cola FEMSA purchases concentrates under the bottler agreements may vary materially from the prices it has historically paid. However, under Coca-Cola FEMSA's bylaws and the shareholders agreement among The Coca-Cola Company and certain of its subsidiaries and certain subsidiaries of our company, an adverse action by The Coca-Cola Company under any of the bottler agreements may result in a suspension of certain veto rights of the directors appointed by The Coca-Cola Company. This provides us with limited protection against The Coca-Cola Company's ability to raise concentrate prices to the extent that such increase is deemed detrimental to Coca-Cola FEMSA pursuant to the shareholder agreement and the bylaws. See Shareholders Agreement.



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The Coca-Cola Company has the ability, at its sole discretion, to reformulate any of the *Coca-Cola* trademark beverages and to discontinue any of the Coca-Cola trademark beverages, subject to certain limitations, so long as all Coca-Cola trademark beverages are not discontinued. The Coca-Cola Company may also introduce new beverages in Coca-Cola FEMSA's territories in which case Coca-Cola FEMSA has a right of first refusal with respect to the manufacturing, packaging, distribution and sale of such new beverages subject to the same obligations as then exist with respect to the *Coca-Cola* trademark beverages under the bottler agreements. The bottler agreements prohibit Coca-Cola FEMSA from producing or handling cola products other than those of The Coca-Cola Company, or other products or packages that would imitate, infringe upon, or cause confusion with the products, trade dress, containers or trademarks of The Coca-Cola Company, or from acquiring or holding an interest in a party that engages in such activities. The bottler agreements also prohibit Coca-Cola FEMSA from bottling any soft drink product except under the authority of, or with the consent of, The Coca-Cola Company. The bottler agreements impose restrictions concerning the use of certain trademarks, authorized containers, packaging and labeling of The Coca-Cola Company so as to conform to policies prescribed by The Coca-Cola Company. In particular, Coca-Cola FEMSA is obligated to:

maintain plant and equipment, staff and distribution facilities capable of manufacturing, packaging and distributing the Coca-Cola trademark beverages in authorized containers in accordance with Coca-Cola FEMSA bottler agreements and in sufficient quantities to satisfy fully the demand in its territories;

undertake adequate quality control measures prescribed by The Coca-Cola Company;

develop, stimulate and satisfy fully the demand for *Coca-Cola* trademark beverages using all approved means, which includes the investment in advertising and marketing plans;

maintain a sound financial capacity as may be reasonably necessary to assure performance by Coca-Cola FEMSA and its affiliates of their obligations to The Coca-Cola Company; and

submit annually to The Coca-Cola Company, Coca-Cola FEMSA's marketing, management, promotional and advertising plans for the ensuing year.

The Coca-Cola Company contributed a significant portion of Coca-Cola FEMSA's total marketing expenses in its territories during 2006 and has reiterated its intention to continue providing support as part of its new cooperation framework with Coca-Cola FEMSA. Although Coca-Cola FEMSA believes that The Coca-Cola Company will continue to provide funds for advertising and marketing, it is not obligated to do so. Consequently, future levels of advertising and marketing support provided by The Coca-Cola Company may vary materially from the levels historically provided. See Shareholders Agreement.

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Coca-Cola FEMSA has separate bottler agreements with The Coca-Cola Company for each of the territories in which it operates. Some of these bottler agreements renew automatically unless one of the parties gives prior notice that it does not wish to renew the agreement, while others require an agreement between the parties or require Coca-Cola FEMSA to give notice electing to renew the agreement. The following table summarizes by segment the expiration dates and renewal provisions of Coca-Cola FEMSA's bottler agreements:

Segment	Expiration Date	Renewal/Termination Provision
<b>Mexico</b>	For two territories June 2013	10 years, renewable automatically.
	For two territories May 2015	10 years, renewable automatically.
<b>Central America<sup>(1)</sup></b>	Guatemala June 2007	Renewable as agreed between the parties.
	Nicaragua June 2007	Five years, requires notice at least six but not more than 12 months before expiration date.
	Costa Rica September 2007	Five years, requires notice at least six but not more than 12 months before expiration date.
	Panamá (Coca-Cola trademark beverages) Indefinite.	May be terminated by either party with six months prior written notice.
	Panamá (Other beverages) June 2007.	Five years, requires notice at least six but no more than 12 months before expiration date.
<b>Segment</b>	<b>Expiration Date</b>	<b>Renewal Provision</b>
<b>Colombia</b>	June 2007	Five years, requires notice at least six but not more than 12 months before expiration date.
<b>Venezuela</b>	For Coca-Cola trademark beverages August 2006 <sup>(1)</sup>	Five years, requires notice at least six but not more than 12 months before expiration date.
	For other beverages August 2006 <sup>(1)</sup>	Renewable as agreed between the parties.
<b>Brazil</b>	December 2004 <sup>(1)</sup>	Five years, requires notice at least six but not more than 12 months before expiration date.
<b>Argentina</b>	September 2014	10 years, renewable automatically.

(1) Coca-Cola FEMSA is in the process of negotiating renewals for these territories.

The bottler agreements are subject to termination by The Coca-Cola Company in the event of default by Coca-Cola FEMSA. The default provisions include limitations on the change in ownership or control of Coca-Cola FEMSA and the assignment or transfer of the bottler agreements and are designed to preclude any person not acceptable to The Coca-Cola Company from obtaining an assignment of a bottler agreement or from acquiring Coca-Cola FEMSA independently of similar rights set forth in the shareholders agreement. These provisions may prevent changes in Coca-Cola FEMSA's principal shareholders, including mergers or acquisitions involving sales or dispositions of Coca-Cola FEMSA's capital stock, which will involve an effective change of control without the consent of The Coca-Cola Company. See Shareholders Agreement.

Coca-Cola FEMSA has also entered into tradename licensing agreements with The Coca-Cola Company pursuant to which Coca-Cola FEMSA is authorized to use certain trademark names of The Coca-Cola Company. These agreements have an indefinite term, but are terminated if Coca-Cola FEMSA ceases to manufacture, market, sell and distribute Coca-Cola trademark products pursuant to the bottler agreements or if the shareholders agreement is terminated. The Coca-Cola Company also has the right to terminate the license agreement if Coca-Cola FEMSA uses its trademark names in a manner not authorized by the bottler agreements.

**Documents on Display**

We file reports, including annual reports on Form 20-F, and other information with the SEC pursuant to the rules and regulations of the SEC that apply to foreign private issuers. You may read and copy any materials filed with the SEC at its public reference rooms in Washington, D.C., at

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100 F Street, N.W., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. Filings we make electronically with the SEC are also available to the public over the Internet at the SEC's website at [www.sec.gov](http://www.sec.gov).

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**ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Our business activities require the holding or issuing of financial instruments that expose us to market risks related to changes in interest rates, foreign currency exchange rates, equity risk and commodity price risk.

**Interest Rate Risk**

Interest rate risk exists principally with respect to our indebtedness that bears interest at floating rates. At December 31, 2006, we had outstanding long-term indebtedness of Ps. 36,691 million, of which 25.9% bore interest at fixed interest rates and 74.1% bore interest at variable interest rates. Swap contracts held by us effectively switch a portion of our variable rate indebtedness into fixed-rate indebtedness. After giving effect to these contracts, as of December 31, 2006, 80.4% of our long-term indebtedness was fixed rate and 19.6% of our long-term indebtedness was variable rate. The interest rate on our variable rate debt is determined by reference to the London Interbank Offered Rate, or LIBOR (a benchmark rate used for Eurodollar loans), the Tasa de Interés Interbancaria de Equilibrio (Equilibrium Interbank Interest Rate) or TIEE, and the Certificados de la Tesorería (Treasury Certificates) or CETES rate. If these reference rates increase, our interest payments would consequently increase.

The table below provides information about our financial instruments that are sensitive to changes in interest rates. The table presents notional amounts and weighted average interest rates by expected contractual maturity dates. Notional amounts are used to calculate the contractual payments to be exchanged under the contract. Weighted average variable rates are based on the reference rates on December 31, 2006, plus spreads contracted by us. The instruments' actual payments are denominated in U.S. dollars, Mexican pesos, Brazilian reais and Colombian pesos. All of the payments in the table are presented in Mexican pesos, our reporting currency, utilizing the December 31, 2006 exchange rate of 10.8755 Mexican pesos per U.S. dollar, 5.0868 Mexican pesos per Brazilian reais and 0.0049 Mexican pesos per Colombian peso.

The table below also includes the estimated fair value as of December 31, 2006 of:

long-term debt, based on the discounted value of contractual cash flows, in which the discount rate is estimated using rates currently offered for debt with similar terms and remaining maturities;

long-term notes payable, based on quoted market prices; and

interest rate swaps, based on quoted market prices to terminate the contracts as of December 31, 2006.  
As of December 31, 2006, the fair value represents a loss of Ps. 460 million.



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	At December 31, 2006						Carrying Value	Fair Value	At December 31, 2005	
	2007	2008	2009	2010	2011	2012 and thereafter			Carrying Value	Fair Value
(in millions of constant Mexican pesos)										
<b>Long-term debt:</b>										
Fixed rate debt:										
U.S. dollars	100	468	3,287	20			3,875	3,969	5,957	6,225
Interest rate <sup>(1)</sup>	6.9%	7.0%	7.2%	3.4%			6.9%		7.7%	
Mexican pesos	50	50	640	2,200	280	2,416	5,636	5,921	7,347	7,505
Interest rate <sup>(1)</sup>	9.8%	9.7%	9.7%	9.7%	9.7%	9.8%	9.8%		9.6%	
Japanese yen		151					151	151		
Interest rate <sup>(1)</sup>		5.8%					5.8%			
Subtotal	150	669	3,927	2,220	280	2,416	9,662	10,041	13,304	13,730
Variable rate debt:										
U.S. dollars	54	39	30	29	82	2,435	2,669	2,669	2,523	2,523
Interest rate <sup>(1)</sup>	5.7%	5.7%	5.7%	5.7%	5.7%	5.7%	5.7%		4.8%	
Mexican pesos	2,032	5,118	1,478	2,653	3,776	9,070	24,127	24,195	19,088	19,161
Interest rate <sup>(1)</sup>	7.8%	7.8%	7.7%	7.6%	7.6%	7.6%	7.8%		9.3%	
Colombian pesos	166						166	166	401	401
Interest rate <sup>(1)</sup>	9.3%						9.3%		8.7%	
Brazilian reais	38	28	1				67	67	27	27
Interest rate <sup>(1)</sup>	9.3%	8.9%	11.2%				9.3%		6.5%	
Subtotal	2,290	5,185	1,509	2,682	3,858	11,505	27,029	27,097	22,039	22,112
Total debt	2,440	5,854	5,436	4,902	4,138	13,921	36,691	37,138	35,343	35,842
<b>Derivative instruments:</b>										
Cross currency and interest rate swaps										
U.S. dollars to Mexican pesos:										
Variable to fixed									1,561	(182)
Interest pay rate <sup>(1)</sup>									11.1%	
Interest receive rate <sup>(1)</sup>									4.8%	
Japanese yen to Brazilian reais										
Fixed to variable		151					151	4		
Interest pay rate <sup>(1)</sup>		14.0%					14.0%			
Interest receive rate <sup>(1)</sup>		5.8%					5.8%			

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	At December 31, 2006						At December 31, 2005			
	2007	2008	2009	2010	2011	2012 and thereafter	Carrying Value	Fair Value	Carrying Value	Fair Value
(in millions of constant Mexican pesos)										
Interest rate swaps:										
Mexican pesos:										
Variable to fixed	1,981	5,075	1,460	2,634	3,771	5,070	19,991	(889)	16,885	(514)
Interest pay rate <sup>(1)</sup>	9.5%	9.7%	9.8%	9.7%	9.5%	9.3%	9.5%		9.8%	
Interest receive rate <sup>(1)</sup>	7.7%	7.6%	7.4%	7.4%	7.5%	7.6%	7.7%		9.4%	

(1) Weighted average interest rate.

A hypothetical, instantaneous and unfavorable change of one percentage point in the average interest rate applicable to variable-rate liabilities held at December 31, 2006 would increase our interest expense by approximately Ps. 72 million, or 14.0%, over the 12-month period of 2007, assuming no additional debt is incurred during such period, in each case after giving effect to all of our interest swap agreements.

**Foreign Currency Exchange Rate Risk**

Our principal exchange rate risk involves changes in the value of the local currencies, of each country in which we operated, relative to the U.S. dollar. In 2006, the percentage of our consolidated total revenues was denominated as follows:

**Total Revenues by Currency At December 31, 2006**

Country	Currency	% of Consolidated Total Revenues
Mexico	Mexican peso	72.5
Brazil	Real	9.6
Venezuela	Bolivar	5.2
Colombia	Colombian peso	4.5
Argentina	Argentine peso	2.6
United States	U.S. dollar	2.3
Costa Rica	Colon	1.2
Guatemala	Quetzal	0.8
Nicaragua	Cordoba	0.7
Panama	U.S. dollar	0.6

We estimate that a majority of our consolidated costs and expenses are denominated in Mexican pesos for Mexican subsidiaries and in the aforementioned currencies for the foreign subsidiaries, which are all subsidiaries of Coca-Cola FEMSA. Substantially all of our costs and expenses denominated in a foreign currency, other than the functional currency of each country in which we operate, are denominated in U.S. dollars. As of December 31, 2006, 81.1% of our long-term indebtedness was denominated in Mexican pesos, 17.8% was denominated in U.S. dollars, 0.6% was denominated in Brazilian reais and the remaining 0.5% in Colombian pesos. We also have short-term indebtedness which consists of revolving bank loans. Decreases in the value of the different currencies relative to the U.S. dollar will increase the cost of our foreign currency denominated operating costs and expenses, and the debt service obligations with respect to our foreign currency denominated indebtedness. A depreciation of the Mexican peso relative to the U.S. dollar will also result in foreign exchange losses as the Mexican peso value of our foreign currency denominated long-term indebtedness is increased.

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Our exposure to market risk associated with changes in foreign currency exchange rates relates primarily to U.S. dollar-denominated debt obligations as shown in the interest risk table above. We occasionally utilize financial derivative instruments to hedge our exposure to the U.S. dollar relative to the Mexican peso and other currencies.

As of December 31, 2006, we did not have any forward agreements that meet the hedging criteria for accounting purposes, to hedge our operations denominated in U.S. dollars. During 2005, we had forward agreements for the purchase of U.S. dollars that meet hedging accounting criteria, in a notional amount of US\$250 million, to hedge the foreign exchange rate risk related to our acquisition of a 30% interest in FEMSA Cerveza. These contracts were paid during 2005, and we recognized a foreign exchange loss of Ps. 162 million.

Additionally, as of December 31, 2006, we had certain forward contracts that did not meet the hedging criteria for accounting purposes; consequently, changes in the fair value of Ps. 22 million were recorded in the income statement. These contracts, which have a notional amount of Ps. 1,144 million, mature in June and August 2007. The fair value of the foreign currency forward contracts is estimated based on the quoted market price of each agreement at year-end assuming the same maturity dates originally contracted.

As of December 31, 2006, we had forward agreements to buy euros to hedge the exchange risk between the U.S. dollar and the euro for the purchase of equipment. These contracts with a notional amount of 2 million, mature in 2007 and represented a loss of Ps. 2 million, Ps. 9 million and Ps. 18 million for the years ended December 31, 2006, 2005, and 2004, respectively.

As of December 31, 2006, we did not have any call option agreements to buy U.S. dollars. We contracted cross currency swaps to manage the interest rate and foreign exchange risks associated with our borrowings denominated in U.S. dollars and other foreign currencies. The aggregate notional amounts are Ps. 102 million with maturity dates in 2007. The fair value is estimated based on quoted market exchange rates and interest rates to terminate the contracts at December 31, 2006, with a fair value liability of Ps. 18 million. The net effect of expired contracts is included in interest expense and amounted to Ps. 70 million.

As of December 31, 2006, certain cross currency swap instruments do not meet the hedging criteria for accounting purposes; consequently changes in the estimated fair value were recorded in the income statement. These contracts with a notional amount of Ps. 2,843 million mature in December 2011 with a fair value liability of Ps. 47 million.

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	Forward Agreements			
	At December 31, 2006		At December 31, 2005	
	Notional	Fair Value	Notional	Fair Value
	Amount	(in millions of U.S. dollars)	Amount	(in millions of U.S. dollars)
				constant " Mexican pesos)

**Euro forwards:**

To cover Mexican peso risk	2	Ps.2		
Weighted average foreign exchange rate Mexican peso per Euro:				
Contracted	13.0470			
Quoted market	14.3303			
<b>Cross currency and interest rate swap:</b>				
To cover Japanese yen risk	¥ 4,267	Ps.(18)		
Weighted average foreign exchange rate Brazilian reais per Japanese yen:				
Contracted	0.0185			
Quoted market	0.0181			
To cover U.S. dollar risk			\$ 140	Ps.(175)
Weighted average foreign exchange rate Mexican peso per U.S. dollar:				
Contracted			11.0049	
Quoted market			10.7109	

As of December 31, 2006, we had determined that our leasing contracts denominated in U.S. dollars host an embedded derivative financial instrument. At December 31, 2006 and 2005, the fair value of these contracts represented Ps. 67 million and Ps. 124 million, respectively, which are recorded in the income statement as market value loss on ineffective portion of derivative financial instruments.

A hypothetical, instantaneous and unfavorable 10% devaluation in the value of the Mexican peso relative to the U.S. dollar occurring on December 31, 2006, would have resulted in an increase in our net consolidated integral result of financing expense of approximately Ps. 585 million over the 12-month period of 2007, reflecting higher interest expense and foreign exchange gain generated by the cash balances held in U.S. dollars as of that date, net of the loss based on our U.S. dollar-denominated indebtedness at December 31, 2006. However, this result does not take into account any gain on monetary position that would be expected to result from an increase in the inflation rate generated by a devaluation of the Mexican peso relative to the U.S. dollar, which gain on monetary position would reduce the consolidated net integral cost of financing.

As of March 31, 2007, the exchange rates relative to the U.S. dollar of all the countries in which we operate as well as their devaluation/revaluation effect compared to December 31, 2006, are as follows:

Country	Currency	Exchange Rate at March 31, 2007	(Devaluation) / Revaluation
Mexico	Mexican peso	11.0507	(1.6)%
Brazil	Real	2.0504	4.1%
Venezuela	Bolivar	2,150.0000	
Colombia	Colombian peso	2,190.3000	2.2%
Argentina	Argentine peso	3.1000	(1.2)%
Costa Rica	Colon	520.6900	(0.1)%
Guatemala	Quetzal	7.6924	(1.3)%
Nicaragua	Cordoba	18.2207	(1.2)%
Panama	U.S. dollar	1.0000	

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A hypothetical, instantaneous and unfavorable 10% devaluation in the value of the currencies of all the countries in which we operate, relative to the U.S. dollar occurring on December 31, 2006, would produce a reduction in stockholders' equity as follows:

Country	Currency	Reduction in Stockholders' Equity (in millions of Mexican pesos)
Mexico	Mexican peso	2,049
Argentina	Argentine peso	58
Brazil	Real	428
Venezuela	Bolivar	201
Colombia	Colombian peso	686
Costa Rica	Colon	181
Guatemala	Quetzal	57
Nicaragua	Cordoba	78
Panama	U.S. dollar	

**Equity Risk**

During 2002, one of Coca-Cola FEMSA's subsidiaries entered into an equity forward sale contract, with a notional amount of approximately Ps. 221 million. This contract expired in 2004 and Coca-Cola FEMSA recorded a loss on this instrument of Ps. 81 million, which resulted from the difference between the strike price of the forward contract and the market value of the shares.

As of December 31, 2006 and 2005, we did not have any equity forward agreements.

**Commodity Price Risk**

We entered into various derivative contracts to hedge the cost of certain raw materials. The result of our commodity price contracts was a loss of Ps. 104 million and a loss of Ps. 2 million for the years ended December 31, 2006 and 2005, respectively, which were recorded in the results of operations of the year. The fair value is estimated based on the quoted market prices to terminate the contracts at the reporting date. As of December 31, 2006, we had various derivative instruments contracts with maturity dates in 2008 and 2010, notional amounts of Ps. 1,029 million and a fair value loss of Ps. 75 million.

**ITEMS 12-14. NOT APPLICABLE****ITEM 15. CONTROLS AND PROCEDURES****(a) Disclosure Controls and Procedures**

We have evaluated, with the participation of our chief executive officer and chief financial officer, the effectiveness of our disclosure controls and procedures as of December 31, 2006. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based upon our evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and

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procedures were effective to provide reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the applicable rules and forms, and that it is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

**(b) Management's Annual Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended. Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on our financial statements.

We have excluded from our assessment the internal control over financial reporting at Cevejarias Kaiser Brasil, S.A., which was acquired on January 13, 2006. Kaiser constitutes 3% of total assets, total revenues and net income of the consolidated financial statement amounts as of and for the year ended December 31, 2006.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Based on our evaluation under the framework in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission, our management concluded that our internal control over financial reporting was effective as of December 31, 2006.

Our management's assessment of the effectiveness of our internal control over financial reporting as of December 31, 2006 has been audited by Galaz, Yamazaki, Ruiz Urquiza, S.C., a member of Deloitte Touche Tohmatsu and an independent registered public accounting firm, as stated in their report included herein.

**(c) Attestation Report of the Registered Public Accounting Firm**

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS OF

FOMENTO ECONÓMICO MEXICANO, S.A.B. DE C.V.

Monterrey, N.L., Mexico

We have audited management's assessment, included in the accompanying Management's Annual Report on Internal Control over Financial Reporting, that Fomento Económico Mexicano, S.A.B. de C.V. (formerly Fomento Económico Mexicano, S.A. de C.V., a Mexican corporation) and subsidiaries (the Company) maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. As described in Management's Annual Report on Internal Control over Financial

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Reporting, management excluded from its assessment the internal control over financial reporting at Cevejarias Kaiser Brasil, S.A. ( Kaiser ), which was acquired on January 13, 2006. Kaiser constitutes 3% of total assets, total revenues and net income of the consolidated financial statement amounts as of and for the year ended December 31, 2006. Accordingly, our audit did not include the internal control over financial reporting at Kaiser.

The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management s assessment and an opinion on the effectiveness of the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management s assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed by, or under the supervision of, the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management s assessment that the Company maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2006 of the Company, and our report dated June 26, 2007 expressed an unqualified opinion on those financial statements and includes explanatory paragraphs regarding (1) the nature and effect of differences between Mexican Financial Reporting Standards and accounting principles generally accepted in the United States of America (2) the adoption of Statement of Financial Accounting Standards No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R)* and (3)

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that our audit also comprehended the translation of Mexican peso amounts into U.S. dollar amounts in conformity with the basis stated in Note 2 to such consolidated financial statements.

Galaz, Yamazaki, Ruiz Urquiza, S.C.

Member of Deloitte Touche Tohmatsu

C.P.C. Gabriel González Martínez

Monterrey, N.L., Mexico

June 26, 2007

**(d) Changes in Internal Control over Financial Reporting**

During 2006, there were no changes in the Company's internal control over financial reporting that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT**

Our shareholders and our board of directors have designated José Manuel Canal Hernando, an independent director as required by the Mexican Securities Market Law and applicable New York Stock Exchange listing standards, as an audit committee financial expert within the meaning of this Item 16A. See Item 6. Directors, Senior Management and Employees Directors.

**ITEM 16B. CODE OF ETHICS**

We have adopted a code of ethics, within the meaning of this Item 16B of Form 20-F. Our code of ethics applies to our chief executive officer, chief financial officer, chief accounting officer and persons performing similar functions as well as to our directors and other officers and employees. Our code of ethics is available on our website at [www.femsa.com/ethics.asp](http://www.femsa.com/ethics.asp). If we amend the provisions of our code of ethics that apply to our chief executive officer, chief financial officer, chief accounting officer and persons performing similar functions, or if we grant any waiver of such provisions, we will disclose such amendment or waiver on our web site at the same address.

**ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES****Audit and Non-Audit Fees**

The following table summarizes the aggregate fees billed to us by Galaz, Yamazaki, Ruiz Urquiza, S.C., Member of Deloitte Touche Tohmatsu, and its affiliates as principal auditors, which we collectively refer to as Deloitte, during the fiscal years ended December 31, 2006 and 2005:

	<b>Year ended December 31,</b>	
	<b>2006</b>	<b>2005</b>
	<b>(in millions of Mexican pesos)</b>	
Audit fees	Ps. 101	Ps. 64
Audit-related fees	15	8
Tax fees	5	6
Other fees	6	
<b>Total</b>	<b>Ps. 127</b>	<b>Ps. 78</b>

*Audit fees.* Audit fees in the above table are the aggregate fees billed by Deloitte in connection with the audit of our annual financial statements, the review of our quarterly financial statements, statutory and regulatory audits and compliance by FEMSA with Section 404 of the Sarbanes-Oxley Act of 2002.



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*Audit-related fees.* Audit-related fees in the above table for the year ended December 31, 2006 are the aggregate fees billed by Deloitte for financial accounting and reporting-related matters relating to the review of the prospectus for the equity offering.

*Tax fees.* Tax fees in the above table are fees billed by Deloitte for services based upon existing facts and prior transactions in order to document, compute, and obtain government approval for amounts included in tax filings such as value-added tax return assistance, transfer pricing documentation and requests for technical advice from taxing authorities.

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*Other fees.* Other fees in the above table are consulting related fees. As a percentage of the total fees billed to us, other fees represents 5% for 2006.

**Audit Committee Pre-Approval Policies and Procedures**

We have adopted pre-approval policies and procedures under which all audit and non-audit services provided by our external auditors must be pre-approved by the Audit Committee as set forth in the Audit Committee's charter. Any service proposals submitted by external auditors need to be discussed and approved by the Audit Committee during its meetings, which take place at least four times a year. Once the proposed service is approved, we or our subsidiaries formalize the engagement of services. The approval of any audit and non-audit services to be provided by our external auditors is specified in the minutes of our Audit Committee. In addition, the members of our board of directors are briefed on matters discussed by the different committees of our board.

**ITEM 16D. NOT APPLICABLE**

**ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS**

We did not purchase any of our equity securities in 2006. The following table presents purchases by trusts that we administer in connection with our stock incentive plans, which purchases may be deemed to be purchases by an affiliated purchaser of us. See Item 6. Directors, Senior Management and Employees Stock Incentive Plan and EVA Stock Incentive Plan.

**Table of Contents****Purchases of Equity Securities**

<b>Purchase Date</b>	<b>Total Number of BD Units Purchased</b>	<b>Average Price Paid per BD Units</b>	<b>Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Maximum Number (or Appropriate U.S. Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs</b>
March 23, 2006	687,610	Ps.95.42		
March 1, 2007	1,067,380	Ps.123.50		

**ITEM 17. NOT APPLICABLE****ITEM 18. FINANCIAL STATEMENTS**

See pages F-1 through F-54, incorporated herein by reference.

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**ITEM 19 EXHIBITS**

- 1.1 Amended and Restated Bylaws (*Estatutos Sociales*) of FEMSA, dated December 7, 2006.
- 2.1 Deposit Agreement, as further amended and restated, among FEMSA, The Bank of New York, and all owners and holders from time to time of any American Depositary Receipts, including the form of American Depositary Receipt (incorporated by reference to FEMSA's registration statement on Form F-6 filed on April 30, 2007 (File No. 333-142469)).
- 2.2 Specimen certificate representing a BD Unit, consisting of one Series B Share, two Series D-B Shares and two Series D-L Shares, together with an English translation (incorporated by reference to FEMSA's registration statement on Form F-4 filed on April 9, 1998 (File No. 333-8618)).
- 2.3 Indenture, dated July 11, 1997, by and between Corporación Interamericana de Bebidas, S.A. de C.V. and The Chase Manhattan Bank, as Trustee (incorporated by reference to Exhibit 4.1 of Panamco's Registration Statement on Form F-4, (File No. 333-7918)).
- 2.4 First Supplemental Indenture, dated October 15, 2003, between Corporación Interamericana de Bebidas, S.A. de C.V., as Issuer, Coca-Cola FEMSA, as Guarantor, and JPMorgan Chase Bank, as Trustee (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-2260)).
- 2.5 Second Supplemental Indenture, dated November 19, 2003, between Corporación Interamericana de Bebidas, S.A. de C.V., as Issuer, Coca-Cola FEMSA, as Guarantor, and JPMorgan Chase Bank, as Trustee (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-2260)).
- 2.6 Credit Agreement, dated as of September 27, 2004, among FEMSA Comercio, as borrower, Cadena Comercial Oxxo, S.A. de C.V., Impulsora de Mercados de Mexico, S.A. de C.V. and Oxxo Express, S.A. de C.V., as guarantors, the financial institutions party thereto, as lenders, BBVA Bancomer, S.A., as administrative agent, and BBVA Securities Inc, as mandated lead arranger (incorporated by reference to FEMSA's Annual Report on Form 20-F filed on April 8, 2005 (File No. 333-08752)).
- 3.1 Amended Voting Trust Agreement among certain principal shareholders of FEMSA together with an English translation (incorporated by reference to FEMSA's Schedule 13D as amended filed on August 11, 2005 (File No. 005-54705)).
- 4.1 Amended and Restated Shareholders Agreement, dated July 6, 2002, among CIBSA, Emprex, The Coca-Cola Company and Inmex (incorporated by reference to Coca-Cola FEMSA's annual report on Form 20-F filed on June 27, 2003 (File No. 1-12260)).
- 4.2 Amendment, dated May 6, 2003, to Shareholders Agreement as amended and restated on July 6, 2002, among CIBSA, Emprex, The Coca-Cola Company, Inmex, Atlantic Industries, Dulux CBAI 2003 B.V. and Dulux CBEXINMX 2003 B.V. (incorporated by reference to Coca-Cola FEMSA's annual report on Form 20-F filed on June 27, 2003 (File No. 1-12260)).
- 4.3 Amended and Restated Bottler Agreement, dated June 21, 2003, between Coca-Cola FEMSA and The Coca-Cola Company with respect to operations in the valley of Mexico (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).

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- 4.4 Supplemental Agreement, dated June 21, 1993, between Coca-Cola FEMSA and The Coca-Cola Company with respect to operations in the valley of Mexico (with English translation) (incorporated by reference to Exhibit 10.3 to Coca-Cola FEMSA's Registration Statement on Form F-1 filed on August 13, 1993 (File No. 333-67380)).
- 4.5 Amended and Restated Bottler Agreement, dated June 21, 2003, between Coca-Cola FEMSA and The Coca-Cola Company with respect to operations in the southeast of Mexico (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).
- 4.6 Bottler Agreement, dated August 22, 1994, between Coca-Cola FEMSA and The Coca-Cola Company with respect to operations in Argentina (with English translation) (incorporated by reference to Exhibit 10.1 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 30, 1995 (File No. 1-12260)).
- 4.7 Supplemental Agreement, dated August 22, 1994, between Coca-Cola FEMSA and The Coca-Cola Company with respect to operations in Argentina (with English translation) (incorporated by reference to Exhibit 10.2 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 30, 1995 (File No. 1-12260)).
- 4.8 Amendments, dated May 17 and July 20, 1995, to Bottler Agreement and Letter of Agreement, dated August 22, 1994, each with respect to operations in Argentina between Coca-Cola FEMSA and The Coca-Cola Company (with English translation) (incorporated by reference to Exhibit 10.3 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 28, 1996 (File No. 1-12260)).
- 4.9 Bottler Agreement, dated December 1, 1995, between Coca-Cola FEMSA and The Coca-Cola Company with respect to operations in SIRSA (with English translation) (incorporated by reference to Exhibit 10.4 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 28, 1996 (File No. 1-12260)).
- 4.10 Supplemental Agreement, dated December 1, 1995, between Coca-Cola FEMSA and The Coca-Cola Company with respect to operations in SIRSA (with English translation) (incorporated by reference to Exhibit 10.6 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 28, 1996 (File No. 1-12260)).
- 4.11 Amendment, dated February 1, 1996, to Bottler Agreement between Coca-Cola FEMSA and The Coca-Cola Company with respect to operations in SIRSA, dated December 1, 1995 (with English translation) (incorporated by reference to Exhibit 10.5 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 28, 1996 (File No. 1-12260)).
- 4.12 Supplemental Agreement, dated June 21, 1993, between Coca-Cola FEMSA and The Coca-Cola Company with respect to operations in the southeast of Mexico (with English translation) (incorporated by reference to Exhibit 10.4 to Coca-Cola FEMSA's Registration Statement on Form F-1 filed on August 13, 1993 (File No. 333-67380)).
- 4.13 Amendment, dated May 22, 1998, to Bottler Agreement with respect to the former SIRSA territory, dated December 1, 1995, between Coca-Cola FEMSA and The Coca-Cola Company (with English translation) (incorporated by reference to Exhibit 4.12 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 20, 2001 (File No. 1-12260)).

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- 4.14 Bottler Agreement and Letter Agreement, each dated March 18, 2000, between The Coca-Cola Company and Embotelladora Central, S.A. with respect to operations in Guatemala (English translation) (incorporated by reference to Exhibit 4.9 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).
- 4.15 Bottler Agreement and Letter Agreement, each dated May 13, 2001, between The Coca-Cola Company and Panamco de Nicaragua, S.A. with respect to operations in Nicaragua (English translation) (incorporated by reference to Exhibit 4.10 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).
- 4.16 Letter of Renewal, dated January 1, 2007, between The Coca-Cola Company and Industria Nacional de Refrescos, S.A., with respect to operations in Nicaragua (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 25, 2007 (File No. 1-12260)).
- 4.17 Bottler Agreement, dated August 1, 1947, between The Coca-Cola Company and The Panama Coca-Cola Bottling Company, with respect to operations in Panama (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 25, 2007 (File No. 1-12260)).
- 4.18 Bottler Agreement, dated November 1, 1994 between The Coca-Cola Company and Coca-Cola de Panamá, Compañía Embotelladora, S.A. with respect to operations in Panama (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 25, 2007 (File No. 1-12260)).
- 4.19 Bottler Agreement and Letter Agreement, each dated October 1, 2002, between The Coca-Cola Company and Embotelladora Panamco Tica, S.A. with respect to operations in Costa Rica (English translation) (incorporated by reference to Exhibit 4.11 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).
- 4.20 Bottler Agreement, dated July 1, 1999, between The Coca-Cola Company and Panamco-Colombia, S.A., with respect to operations in Colombia (English translation) (incorporated by reference to Exhibit 4.12 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).
- 4.21 Bottler Agreement, dated August 16, 1996, and Letter of Renewal, dated February 9, 2001, between The Coca-Cola Company and Embotelladora Coca-Cola y Hit de Venezuela, S.A. with respect to operations in Venezuela (with English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).
- 4.22 Bottler Agreement, dated August 16, 1996, and Letter of Renewal, dated February 9, 2001, between Advantage Investments, Inc. and Embotelladora Coca-Cola y Hit de Venezuela, S.A. with respect to operations in Venezuela (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).
- 4.23 Supply Agreement, dated June 21, 1993, between Coca-Cola FEMSA and FEMSA Empaques (incorporated by reference to FEMSA's registration statement on Form F-4 filed on April 9, 1998 (File No. 333-8618)).

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- 4.24 Bottler Agreement and Side Letter dated June 1, 2005, between Panamco Golfo, S.A. de C.V. and The Coca-Cola Company with respect to operations in Golfo, Mexico (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 18, 2006 (File No. 1-12260)).
- 4.25 Bottler Agreement and Side Letter dated June 1, 2005, between Panamco Bajio, S.A. de C.V., and the Coca-Cola Company with respect to operations in Bajio, Mexico (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 18, 2006 (File No. 1-12260)).
- 4.26 Letter of Renewal, dated January 1, 2007, between The Coca-Cola Company and Embotelladora Central, S.A., with respect to operations in Guatemala (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 25, 2007 (File No. 1-12260)).
- 4.27 Letter of Renewal, dated January 1, 2007, between The Coca-Cola Company and Coca-Cola FEMSA de Panamá, S.A. with respect to operations in Panama (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 25, 2007 (File No. 1-12260)).
- 4.28 Manufacturing Agreement, dated April 16, 1999, between Coca-Cola Industrias Ltda., SPAL Industria Brasileira de Bebidas, S.A. and The Coca-Cola Company with respect to operations in São Paulo, Brazil (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).
- 4.29 Manufacturing Agreement, dated April 16, 1999, between Coca-Cola Industrias Ltda., SPAL Industria Brasileira de Bebidas, S.A. and The Coca-Cola Company with respect to operations in Campinas, Brazil (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).
- 4.30 Manufacturing Agreement, dated April 16, 1999, between Coca-Cola Industrias Ltda., SPAL Industria Brasileira de Bebidas, S.A., and The Coca-Cola Company with respect to operations in Campo Grande, Brazil (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on April 5, 2004 (File No. 1-12260)).
- 4.31 Coca-Cola Tradename License Agreement dated June 21, 1993, between Coca-Cola FEMSA and The Coca-Cola Company (with English translation) (incorporated by reference to FEMSA's Registration Statement on Form F-4 filed on April 9, 1998 (File No. 333-8618)).
- 4.32 Amendment to the Trademark License Agreement, dated December 1, 2002, entered by and among Administracion de Marcas S.A. de C.V., as proprietor, and The Coca-Cola Export Corporation Mexico branch, as licensee (incorporated by reference to Panamco's Quarterly Report on Form 10-Q for the period ended March 31, 2003 (File No. 1-2290)).
- 4.33 Trademark Sub-License Agreement, dated January 4, 2003, entered by and among Panamco Golfo S.A. de C.V., as licensor, and The Coca-Cola Company, as licensee (incorporated by reference to Panamco's Quarterly Report on Form 10-Q for the period ended March 31, 2003 (File No. 1-2290)).
- 4.34 Trademark Sub-License Agreement, dated January 4, 2003, entered by and among Panamco Bajio S.A. de C.V., as licensor, and The Coca-Cola Company, as licensee (incorporated by reference to Panamco's Quarterly Report on Form 10-Q for the period ended March 31, 2003 (File No. 1-2290)).

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- 4.35 Supply Agreement dated April 3, 1998, between ALPLA Fábrica de Plásticos, S.A. de C.V. and Industria Embotelladora de México, S.A. de C.V. (with English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on July 1, 2002 (File No. 1-12260)).
- 4.36 Services Agreement, dated November 7, 2000, between Coca-Cola FEMSA and FEMSA Logística, S.A. de C.V. (with English translation) (incorporated by reference to Exhibit 4.15 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 20, 2001 (File No. 1-12260)).
- 4.37 Promotion and Non-Compete Agreement, dated March 11, 2003, entered by and among The Coca-Cola Export Corporation Mexico branch and Panamco Bajío S.A. de C.V. (with English translation) (incorporated by reference to Panamco's Quarterly Report on Form 10-Q for the period ended March 31, 2003 (File No. 1-2290)).
- 4.38 Promotion and Non-Compete Agreement, dated March 11, 2003, entered by and among The Coca-Cola Export Corporation Mexico branch and Panamco Golfo S.A. de C.V. (with English translation) (incorporated by reference to Panamco's Quarterly Report on Form 10-Q for the period ended March 31, 2003 (File No. 1-2290)).
- 4.39 Memorandum of Understanding, dated as of March 11, 2003, by and among Panamco, as seller, and The Coca-Cola Company, as buyer (incorporated by reference to Panamco's Quarterly Report on Form 10-Q for the period ended March 31, 2003 (File No. 1-2290)).
- 4.40 Letter of Renewal, dated January 1, 2007, between The Coca-Cola Company and Industria Nacional de Gaseosas S.A., with respect to operations in Colombia (English translation) (incorporated by reference to Coca-Cola FEMSA's Annual Report on Form 20-F filed on June 25, 2007 (File No. 1-12260)).
- 4.41 Coca-Cola Tradename License Agreement dated June 21, 1993, between Coca-Cola FEMSA and The Coca-Cola Company (with English translation) (incorporated by reference to Exhibit 10.40 to FEMSA's Registration Statement on Form F-4 filed on April 9, 1998 (File No. 333-8618)).
- 4.42 Supply Agreement dated April 3, 1998, between ALPLA Fábrica de Plásticos, S.A. de C.V. and Industria Embotelladora de México, S.A. de C.V. (with English translation) (incorporated by reference to Exhibit 4.18 to Coca-Cola FEMSA's Annual Report on Form 20-F filed on July 1, 2002 (File No. 1-12260)).
- 4.43 Share Purchase Agreement, dated November 3, 2006, between Compañía Internacional de Bebidas, S.A. de C.V., The Inmex Corporation and Dulux CBEXINMEX 2003 B.V.
- 8.1 Significant Subsidiaries.
- 10.1 The Coca-Cola Company Memorandum, to Steve Heyer from José Antonio Fernández, dated December 22, 2002 (incorporated by reference to FEMSA's registration statement on Form F-3 filed on September 20, 2004 (File No. 333-117795)).
- 12.1 CEO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated June 28, 2006.
- 12.2 CFO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated June 28, 2006.
- 13.1 Officer Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated June 28, 2006.



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**SIGNATURE**

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

Date: June 28, 2007

Fomento Económico Mexicano, S.A. de C.V.

By: /s/ JAVIER ASTABURUAGA SANJINES

**Name: Javier Astaburuaga Sanjines**

**Title: Executive Vice-President of Finance and Strategic Development**

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**FOMENTO ECONÓMICO, S.A.B. DE C.V. AND SUBSIDIARIES**

**MONTERREY, N.L., MEXICO**

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**Report of Independent Registered Public Accounting Firm**

**To the Board of Directors and Stockholders of**

**Fomento Económico Mexicano, S.A.B. de C.V.:**

We have audited the accompanying consolidated balance sheets of Fomento Económico Mexicano, S.A.B. de C.V. (formerly Fomento Económico Mexicano, S.A. de C.V., a Mexican corporation) and subsidiaries (the Company) as of December 31, 2006 and 2005, and the related consolidated statements of income, changes in stockholders' equity and changes in financial position for each of the three years in the period ended December 31, 2006, all expressed in millions of Mexican pesos of purchasing power as of December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of FEMSA Comercio, S.A. de C.V. and subsidiaries (a consolidated subsidiary), which statements reflect total assets constituting 8% and 7%, respectively, of consolidated total assets at December 31, 2006 and 2005, and total revenues constituting 28%, 27% and 24%, respectively, of consolidated total revenues for each of the three years in the period ended December 31, 2006. Those statements were audited by other auditors whose report has been furnished to us and our opinion, insofar as it relates to the amounts included for FEMSA Comercio, S.A. de C.V. and subsidiaries, is based solely on the report of the other auditors.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of the other auditors, such consolidated financial statements present fairly, in all material respects, the financial position of Fomento Económico Mexicano, S.A.B. de C.V. and subsidiaries as of December 31, 2006 and 2005, and the results of their operations, changes in their stockholders' equity and changes in their financial position for each of the three years in the period ended December 31, 2006, in conformity with Mexican financial reporting standards.

Mexican financial reporting standards vary in certain significant respects from accounting principles generally accepted in the United States of America. The application of the latter would have affected the determination of net income for each of the three years in the period ended December 31, 2006, and the determination of stockholders' equity as of December 31, 2006 and 2005, to the extent summarized in Note 28.

As disclosed in Note 27 K) to the accompanying consolidated financial statements, the Company adopted the recognition and disclosure provisions of Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R), effective December 31, 2006.

Our audits also comprehended the translation of the Mexican peso amounts into U.S. dollar amounts and, in our opinion, such translation has been made in conformity with the basis stated in Note 2. The translation of the financial statement amounts into U.S. dollars and the translation of the financial statements into English have been made solely for the convenience of readers in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of December 31, 2006, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated June 26, 2007 expressed an unqualified opinion on management's assessment of the effectiveness of the Company's internal control over financial reporting and an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

Galaz, Yamazaki, Ruiz Urquiza, S.C.

Member of Deloitte Touche Tohmatsu

C.P.C. Gabriel González Martínez

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Monterrey, N.L., Mexico

June 26, 2007

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**Table of Contents****FOMENTO ECONÓMICO MEXICANO, S.A.B. DE C.V. AND SUBSIDIARIES****MONTERREY, N.L., MEXICO****Consolidated Balance Sheets**

At December 31, 2006 and 2005. Amounts expressed in millions of U.S. dollars (\$) and in millions of constant Mexican pesos (Ps.) as of December 31, 2006.

	2006		2005
<b>ASSETS</b>			
<b>Current Assets:</b>			
Cash and cash equivalents	\$ 735	Ps. 7,936	Ps. 8,558
Accounts receivable	646	6,974	5,519
Inventories	753	8,129	7,090
Recoverable taxes	111	1,204	952
Other current assets	108	1,166	983
Total current assets	2,353	25,409	23,102
Investments in shares	71	768	800
Property, plant and equipment	4,573	49,390	45,582
Intangible assets	5,170	55,833	50,990
Other assets	876	9,452	7,902
Bottles and cases	260	2,811	2,546
Deferred income tax asset	160	1,727	1,390
<b>TOTAL ASSETS</b>	<b>\$ 13,463</b>	<b>Ps. 145,390</b>	<b>Ps. 132,312</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>			
<b>Current Liabilities:</b>			
Bank loans	\$ 323	Ps. 3,490	Ps. 762
Interest payable	39	426	418
Current maturities of long-term debt	226	2,440	4,401
Suppliers	1,063	11,475	9,505
Taxes payable	231	2,495	2,088
Accounts payable	326	3,510	2,610
Other current liabilities	138	1,501	1,176
Total current liabilities	2,346	25,337	20,960
<b>Long-Term Liabilities:</b>			
Bank loans and notes payable	3,172	34,251	30,942
Deferred income tax liability	355	3,834	3,533
Labor liabilities	288	3,115	2,556
Contingencies and other liabilities	428	4,625	3,832
Total long-term liabilities	4,243	45,825	40,863
Total liabilities	6,589	71,162	61,823
<b>Stockholders Equity:</b>			
Minority interest in consolidated subsidiaries	1,853	20,008	20,462

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Majority interest:			
Capital stock	477	5,154	5,154
Additional paid-in capital	1,835	19,812	21,440
Retained earnings from prior years	2,869	30,988	26,239
Net income	613	6,622	5,766
Cumulative other comprehensive loss	(773)	(8,356)	(8,572)
Majority interest	5,021	54,220	50,027
Total stockholders equity	6,874	74,228	70,489
<b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>	<b>\$ 13,463</b>	<b>Ps. 145,390</b>	Ps. 132,312

The accompanying notes are an integral part of these consolidated balance sheets.

Monterrey, N.L., Mexico, February 23, 2007.

José Antonio Fernández Carbajal  
Chief Executive Officer

Javier Astaburuaga Sanjines  
Chief Financial Officer

**Table of Contents****FOMENTO ECONÓMICO MEXICANO, S.A.B. DE C.V. AND SUBSIDIARIES****MONTERREY, N.L., MEXICO****Consolidated Income Statements**

For the years ended December 31, 2006, 2005 and 2004. Amounts expressed in millions of U.S. dollars (\$) and in millions of constant Mexican pesos (Ps.) as of December 31, 2006, except per share data.

	2006		2005	2004
Net sales	\$ 11,667	Ps. 125,994	Ps. 111,051	Ps. 101,637
Other operating revenues	40	433	585	679
<b>Total revenues</b>	<b>11,707</b>	<b>126,427</b>	111,636	102,316
Cost of sales	6,291	67,940	59,483	54,190
<b>Gross profit</b>	<b>5,416</b>	<b>58,487</b>	52,153	48,126
Operating expenses:				
Administrative	778	8,400	7,466	7,245
Selling	3,028	32,697	28,284	25,917
	<b>3,806</b>	<b>41,097</b>	35,750	33,162
<b>Income from operations</b>	<b>1,610</b>	<b>17,390</b>	16,403	14,964
Integral result of financing:				
Interest expense	(374)	(4,040)	(4,520)	(4,076)
Interest income	65	707	684	613
Foreign exchange gain (loss)	(20)	(217)	308	(23)
Gain on monetary position	129	1,395	1,169	2,112
Market value loss on ineffective portion of derivative financial instruments	(10)	(109)	(160)	
	<b>(210)</b>	<b>(2,264)</b>	(2,519)	(1,374)
<b>Other expenses, net</b>	<b>(104)</b>	<b>(1,125)</b>	(452)	(856)
<b>Income before taxes and employee profit sharing</b>	<b>1,296</b>	<b>14,001</b>	13,432	12,734
Taxes and employee profit sharing	445	4,806	4,866	2,649
<b>Consolidated net income</b>	<b>\$ 851</b>	<b>Ps. 9,195</b>	Ps. 8,566	Ps. 10,085
Net majority income	613	6,622	5,766	6,411
Net minority income	238	2,573	2,800	3,674
<b>Consolidated net income</b>	<b>\$ 851</b>	<b>Ps. 9,195</b>	Ps. 8,566	Ps. 10,085
Net majority income (U.S. dollars and constant Mexican pesos):				
Per Series B share	\$ 0.09	Ps. 0.99	Ps. 0.90	Ps. 1.08
Per Series D share	0.12	1.24	1.13	1.35

**The accompanying notes are an integral part of these consolidated income statements.**





**Table of Contents****FOMENTO ECONÓMICO MEXICANO, S.A.B. DE C.V. AND SUBSIDIARIES****MONTERREY, N.L., MEXICO****Consolidated Statements of Changes in Financial Position**

For the years ended December 31, 2006, 2005 and 2004. Amounts expressed in millions of U.S. dollars (\$) and in millions of constant Mexican pesos (Ps.) as of December 31, 2006.

	2006		2005	2004
<b>Resources Generated by (Used in) Operating Activities:</b>				
Consolidated net income	\$ 851	Ps. 9,195	Ps. 8,566	Ps. 10,085
Depreciation	426	4,599	4,382	4,125
Amortization and other non-cash charges	280	3,021	2,675	2,724
Impairment of long-lived assets	19	200	81	509
Deferred income tax	1	18	(142)	(1,054)
	<b>1,577</b>	<b>17,033</b>	15,562	16,389
Working capital:				
Accounts receivable	(41)	(442)	(489)	(118)
Inventories	(97)	(1,047)	(364)	(1,359)
Recoverable taxes, net	(47)	(505)	(598)	1,002
Other current assets	(13)	(141)	(84)	120
Suppliers and other current liabilities	139	1,503	694	927
Interest payable	1	8	(6)	(35)
Labor liabilities	(25)	(270)	(378)	(272)
Net resources generated by operating activities	<b>1,494</b>	<b>16,139</b>	14,337	16,654
<b>Resources Generated by (Used in) Investing Activities:</b>				
Acquisition of Coca-Cola FEMSA minority interest	(428)	(4,627)		
Acquisitions by FEMSA Cerveza	(168)	(1,816)		
Property, plant and equipment	(456)	(4,924)	(3,364)	(3,304)
Other assets	(276)	(2,972)	(2,585)	(3,257)
Bottles and cases	(60)	(648)	(515)	(408)
Intangible assets	(28)	(301)	(407)	(539)
Other business acquisitions	(15)	(159)		
Investments in shares	4	46	18	184
Acquisition of FEMSA Cerveza minority interest				(15,860)
Net resources used in investing activities	<b>(1,427)</b>	<b>(15,401)</b>	(6,853)	(23,184)
<b>Resources Generated by (Used in) Financing Activities:</b>				
Bank loans obtained	838	9,063	1,986	26,118
Bank loans paid	(420)	(4,536)	(14,013)	(18,889)
Amortization in real terms of long-term liabilities	(108)	(1,169)	(1,332)	(2,021)
Dividends declared and paid	(130)	(1,406)	(1,063)	(907)
Contingencies and other financing liabilities	(293)	(3,167)	(13)	277
Cumulative translation adjustment	(18)	(197)	(177)	(144)
Issuance of capital stock			8,155	
Capital contribution by Coca-Cola FEMSA s minority interest				634
Net resources generated by (used in) financing activities	<b>(131)</b>	<b>(1,412)</b>	(6,457)	5,068

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Cash and cash equivalents:

Net increase (decrease)	(64)	(674)	1,027	(1,462)
Cash received in acquisition of Kaiser	5	52		
Initial balance	794	8,558	7,531	8,993

Ending balance	\$ 735	Ps. 7,936	Ps. 8,558	Ps. 7,531
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**The accompanying notes are an integral part of these consolidated statements of changes in financial position.**

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**Table of Contents****FOMENTO ECONÓMICO MEXICANO, S.A.B. DE C.V. AND SUBSIDIARIES****MONTERREY, N.L., MEXICO***Consolidated Statements of Changes in Stockholders' Equity*

For the years ended December 31, 2006, 2005 and 2004.

Amounts expressed in millions of constant Mexican pesos (Ps.) as of December 31, 2006.

	Capital Stock	Additional Paid-in Capital	Retained Earnings from Prior Years	Net Income	Cumulative Other Comprehensive Loss	Majority Interest	Minority Interest in Consolidated Subsidiaries	Total Stockholders Equity
<b>Balances at December 31, 2003</b>	<b>Ps. 4,799</b>	<b>Ps. 13,640</b>	<b>Ps. 17,495</b>	<b>Ps. 3,631</b>	<b>Ps. (6,640)</b>	<b>Ps. 32,925</b>	<b>Ps. 20,199</b>	<b>Ps. 53,124</b>
Transfer of prior year net income			3,631	(3,631)				
Dividends declared and paid			(594)			(594)	(313)	(907)
Capital contribution by Coca-Cola FEMSA's minority interest							634	634
Acquisition of FEMSA Cerveza minority interest							(6,383)	(6,383)
Comprehensive income				6,411	(420)	5,991	4,184	10,175
<b>Balances at December 31, 2004</b>	<b>4,799</b>	<b>13,640</b>	<b>20,532</b>	<b>6,411</b>	<b>(7,060)</b>	<b>38,322</b>	<b>18,321</b>	<b>56,643</b>
Transfer of prior year net income			6,411	(6,411)				
Dividend declared and paid			(704)			(704)	(359)	(1,063)
Issuance of capital stock	355	7,800				8,155		8,155
Comprehensive income				5,766	(1,512)	4,254	2,500	6,754
<b>Balances at December 31, 2005</b>	<b>5,154</b>	<b>21,440</b>	<b>26,239</b>	<b>5,766</b>	<b>(8,572)</b>	<b>50,027</b>	<b>20,462</b>	<b>70,489</b>
Transfer of prior year net income			5,766	(5,766)				
Dividends declared and paid			(1,017)			(1,017)	(389)	(1,406)
Kaiser's minority interest							368	368
Acquisition of FEMSA Cerveza minority interest		(77)				(77)	(92)	(169)
Acquisition of Coca-Cola FEMSA minority interest		(1,551)				(1,551)	(3,076)	(4,627)
Comprehensive income				6,622	216	6,838	2,735	9,573
<b>Balances at December 31, 2006</b>	<b>Ps. 5,154</b>	<b>Ps. 19,812</b>	<b>Ps. 30,988</b>	<b>Ps. 6,622</b>	<b>Ps. (8,356)</b>	<b>Ps. 54,220</b>	<b>Ps. 20,008</b>	<b>Ps. 74,228</b>

The accompanying notes are an integral part of these consolidated statements of changes in stockholders' equity.

**Table of Contents****FOMENTO ECONÓMICO MEXICANO, S.A.B. DE C.V. AND SUBSIDIARIES****Notes to the Consolidated Financial Statements**

For the years ended December 31, 2006, 2005 and 2004. Amounts expressed in millions of U.S. dollars (\$) and in millions of constant Mexican pesos (Ps.) as of December 31, 2006.

**Note 1. Activities of the Company.**

Fomento Económico Mexicano, S.A.B. de C.V. ( FEMSA ) is a Mexican holding company. On December 7, 2006, FEMSA changed its name as approved at a general extraordinary stockholders meeting from Fomento Económico Mexicano, S.A. de C.V. to Fomento Económico Mexicano, S.A.B. de C.V. due to a requirement of the Mexican Securities Law Issued on June 28, 2006. This new law requires every company that is listed on the Bolsa Mexicana de Valores, S.A. de C.V. ( BMV Mexican Stock Exchange) to include bursátil (publicly traded) in their legal name or use the letter B after S.A.

The principal activities of FEMSA and its subsidiaries (the Company ), as an economic unit, are carried out by operating subsidiaries and grouped under direct and indirect holding company subsidiaries (the Subholding Companies ) of FEMSA. The following is a description of such activities, together with the ownership interest in each Subholding Company:

<b>Subholding Company</b>	<b>% Ownership</b>	<b>Activities</b>
Coca-Cola FEMSA, S.A.B. de C.V. and Subsidiaries  ( Coca-Cola FEMSA )	53.7%  (63.0% of the voting shares)	Production, distribution and marketing of certain Coca-Cola trademark beverages in Mexico, Guatemala, Nicaragua, Costa Rica, Panama, Colombia, Venezuela, Brazil and Argentina. The Coca-Cola Company indirectly owns 31.6% of Coca-Cola FEMSA s capital stock. In addition, shares representing 14.7% of Coca-Cola FEMSA s capital stock are listed on BMV and The New York Stock Exchange, Inc. ( NYSE ).
FEMSA Cerveza, S.A. de C.V. and Subsidiaries  ( FEMSA Cerveza )	100%	Production, distribution and marketing of beer through its principal operating subsidiary, Cervecería Cuauhtémoc Moctezuma, S.A. de C.V., which operates six breweries throughout Mexico and produces and distributes 18 different brands of beer, of which the five most important are: Tecate, Sol, Carta Blanca, Superior and Indio.  Since January 2006, FEMSA Cerveza produces, distributes and markets beer in Brazil through Cervejarias Kaiser Brasil, S.A. ( Kaiser ) which operates 8 breweries in this country. Kaiser produces 13 different brands of which the most important are Kaiser Pilsen, Bavaria Pilsen and Sol (see Note 6).
FEMSA Comercio, S.A. de C.V. and Subsidiaries  ( FEMSA Comercio )	100%	Operation of a chain of convenience stores in Mexico under the trade name Oxxo.
Other Companies	100%	Companies engaged in the production and distribution of labels, plastic cases, coolers and commercial refrigeration equipment; as well as, transportation logistic and maintenance services to FEMSA s subsidiaries and to third parties.

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### **Note 2. Basis of Presentation.**

The consolidated financial statements include the financial statements of FEMSA and those companies in which it directly or indirectly owns a majority of the outstanding voting capital stock and/or exercises control. All intercompany account balances and transactions have been eliminated in such consolidation.

The consolidated financial statements of the Company are prepared in accordance with Normas de Información Financiera (Mexican Financial Reporting Standards or Mexican FRS), which differ in certain significant respects from generally accepted accounting principles in the United States of America (U.S. GAAP), as further explained in Note 27. A reconciliation from Mexican FRS to U.S. GAAP is included in Note 28.

As of May 31, 2004, the Mexican Institute of Public Accountants (IMCP) formally transferred the function of establishing and issuing financial reporting standards to the Mexican Board for Research and Development of Financial Reporting Standards (CINIF), consistent with the international trend requiring this function be performed by an independent entity. Accordingly, the task of establishing generally accepted accounting principles in Mexico, which included bulletins and circulars issued by the IMCP was transferred to CINIF.

The consolidated financial statements are stated in millions of Mexican pesos (Ps.). The translation of Mexican pesos into U.S. dollars (\$) are included solely for the convenience of the reader, using the noon buying rate exchange rate published by Bank of New York of 10.7995 pesos per U.S. dollar as of December 31, 2006.

The results of the operations acquired by FEMSA are included in the consolidated financial statements since the date of acquisition. During 2006, FEMSA Cerveza acquired some businesses and FEMSA acquired 8.02% of Coca-Cola FEMSA; as a result, the consolidated financial statements are not comparable to the figures presented in prior years (see Note 5 and 6).

On February 23, 2007, the Board of Directors of FEMSA, unanimously approved the consolidated financial statements and the accompanying notes, as of and for the year ended December 31, 2006.

### **Note 3. Foreign Subsidiary Incorporation.**

The accounting records of foreign subsidiaries are maintained in local currency and in accordance with local accounting principles of each country. For incorporation into the FEMSA consolidated financial statements, each foreign subsidiary's individual financial statements are adjusted to Mexican FRS and restated to the purchasing power of the local currency applying inflation factors of the country of origin and are subsequently translated into Mexican pesos using the year-end exchange rate.

The variation in the net investment in foreign subsidiaries generated by exchange rate fluctuations is included in the cumulative translation adjustment and is recorded directly in stockholders' equity as part of other comprehensive income.

The accounting treatment for the integral result of financing when the Company designates a net investment in an acquired foreign subsidiary as an economic hedge to finance its acquisition is as follows:

The foreign exchange gain or loss is recorded as part of the cumulative translation adjustment to the extent the net investment in the foreign subsidiary covers the debt, net of taxes. The foreign exchange gain or loss associated with any unhedged portion of such debt is recorded in the integral result of financing; and

The monetary position result is computed using the inflation factors of the country in which the acquired subsidiary is located to the extent the net investment in that subsidiary covers the debt outstanding and is recorded as part of the cumulative translation adjustment. The monetary position result corresponding to the unhedged portion of such debt is calculated using the inflation factors of the country of the company that enters into the financing, and the effect is recorded in the integral result of financing.

As of the date of these consolidated financial statements, the Company has not designated any investment in a foreign subsidiary as an economic hedge.

The monetary position result and exchange gain or loss generated by foreign subsidiaries associated with the financing of intercompany foreign currency denominated balances recorded in the cumulative translation adjustment in stockholders' equity as part of cumulative other

comprehensive income are considered to be long-term investments since settlement is not planned or anticipated in the foreseeable future.

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### **Note 4. Significant Accounting Policies.**

The Company's accounting policies are in accordance with Mexican FRS, which require that the Company's management makes certain estimates and uses certain assumptions to determine the valuation of various items included in the consolidated financial statements. The Company's management believes that the estimates and assumptions used were appropriated as of the date of these consolidated financial statements.

The significant accounting policies are as follows:

#### **a) Recognition of the Effects of Inflation:**

The recognition of the effects of inflation in the financial information consists of:

Restating non-monetary assets such as inventories and fixed assets, including related costs and expenses when such assets are consumed or depreciated;

Restating capital stock, additional paid-in capital and retained earnings by the amount necessary to maintain the purchasing power equivalent in Mexican pesos on the dates such capital was contributed or income generated, through the use of the appropriate inflation factors;

Including in stockholders' equity the cumulative effect of holding non-monetary assets, which is the net difference between changes in the replacement cost of non-monetary assets and adjustments based upon the inflation factors; and

Including in the cost of financing the purchasing power gain or loss from holding monetary items.

The Company restates its consolidated financial statements in currency of constant purchasing power by applying inflation factors of the country of origin and the exchange rate in effect at the date of the most recent balance sheet presented.

#### **b) Cash and Cash Equivalents:**

Cash consists of non-interest bearing bank deposits. Cash equivalents consist principally of short-term bank deposits and fixed-rate investments with brokerage houses valued at the quoted market prices with original maturities of three months or less. As of December 31, 2006 and 2005 cash equivalents amounted to Ps. 4,802 and Ps. 4,797, respectively.

#### **c) Inventories and Cost of Sales:**

The value of inventories is adjusted to replacement cost, without exceeding market value. Advances to suppliers to purchase raw materials are included in the inventory account and are restated by applying inflation factors, considering their average age.

Cost of sales is determined based on replacement cost at the time of sale. Cost of sales includes expenses related to raw materials used in the production process, labor (wages and other benefits), depreciation of production facilities and equipment and other costs including fuel, electricity, breakage of returnable bottles in the production process, equipment maintenance, inspection and inter and intra-plant transfer costs.

#### **d) Other Current Assets:**

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Other current assets are comprised of payments for services that will be received over the next 12 months and the fair market value of derivative financial instruments with maturity dates of less than one year (see Note 4 q).

Prepaid expenses are recorded at historical cost and are recognized in the income statement when the services or benefits are received. Prepaid expenses principally consist of advertising, promotional, leasing and insurance expenses.

Advertising costs consist of television and radio advertising airtime paid in advance, which are generally amortized over a 12-month period based on the transmission of the television and radio spots. The related production costs are recognized in results of operations the first time the advertising is transmitted.

Promotional costs are expensed as incurred, except for those promotional costs related to the launching of new products or presentations. These costs are recorded as prepaid expenses and amortized over the period during which they are estimated to increase sales of the related products or container presentations to normal operating levels, which is generally no longer than one year.

Additionally, as of December 31, 2006, the Company has restricted cash, classified as other current assets, of Ps. 243 denominated in Venezuelan bolivars, and Ps. 7 denominated in Brazilian reais; both were pledged as collateral of accounts payable and are classified in other current assets due to their short-term nature. As of December 31, 2005, the Company had restricted cash of Ps. 84 denominated in Venezuelan bolivars.



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**e) Bottles and Cases:**

Returnable bottles and cases are recorded at acquisition cost and restated to their replacement cost. There are two types of returnable bottles and cases:

Those that are in the Company's control in its facilities, in plant and distribution centers; and

Those that have been placed in the hands of customers.

Through December 31, 2005, FEMSA Cerveza classified returnable bottles and cases as inventories. Beginning on January 1, 2006, FEMSA Cerveza classifies returnable bottles and cases as long-lived assets in accordance with their estimated useful lives. Accounting estimates regarding returnable bottles and cases have not been modified. Returnable bottles and cases of FEMSA Cerveza as of December 31, 2005 have been reclassified in the accompanying consolidated balance sheets and combined with those of Coca-Cola FEMSA.

For financial reporting purposes, breakage of returnable bottles and cases in plant and distribution centers is recorded as an expense as it is incurred. For the years ended December 31, 2006, 2005 and 2004 breakage expense amounted to Ps. 684, Ps. 765 and Ps. 649 respectively. The Company estimates that breakage expense of returnable bottles and cases in plant and distribution centers is similar to the depreciation calculated on an estimated useful life of approximately five years for beer returnable bottles, four years for soft drinks returnable glass bottles and plastic cases, and 18 months for soft drink returnable plastic bottles.

Depreciation is computed for tax purposes using the straight-line method at a rate of 10% per year. As of January 1, 2005, FEMSA Cerveza, as allowed by the changes to the tax law, modified its tax criteria for the deduction of bottles, from deducting all purchases to computing depreciation using the straight-line method at a rate of 10% per year. The change does not impact the tax provision, but does generate surcharges. The total amount paid in 2005 as a surcharge was Ps. 185, of which Ps. 126 was recorded in net income as of December 31, 2004.

FEMSA Cerveza's returnable bottles and cases are subject to an agreement with a retailer pursuant to which FEMSA Cerveza retains ownership. These bottles and cases are monitored by sales personnel during their periodic visits, and if any breakage is identified, it is charged to the retailer. Bottles and cases that are not subject to such agreements are expensed when placed in the hands of retailers.

Coca-Cola FEMSA's returnable bottles and cases in the market and for which a deposit from customers has been received are presented net of such deposits, and the difference between the cost of these assets and the deposits received is amortized according to their useful lives. The bottles and cases for which no deposit has been received, which represent most of the bottles and cases placed in the market, are expensed when placed in the hands of customers.

**f) Investments in Shares:**

Investments in shares of associated companies are initially recorded at their acquisition cost and subsequently accounted for using the equity method. Investments in affiliated companies in which the Company does not have significant influence are recorded at acquisition cost and are adjusted to market value if they have an observable market value or based upon the inflation factors of the country of origin, with such adjustments reflected in the income statement.

**g) Property, Plant and Equipment:**

Property, plant and equipment are initially recorded at their cost of acquisition and/or construction. Property, plant and equipment of domestic origin are restated by applying inflation factors. Imported equipment is restated by applying inflation factors of the country of origin and then translated at the year-end exchange rate.

Depreciation is computed using the straight-line method, based on the value of the restated assets reduced by their residual values. The Company, together with independent appraisers, estimates depreciation rates, considering the estimated remaining useful lives of the assets.

Through 2005 refrigeration equipment at Coca-Cola FEMSA was amortized on an estimated average useful life of approximately five years.

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During 2006, Coca-Cola FEMSA changed its accounting estimate regarding the useful life of its refrigeration equipment in Mexican territories from 5 to 7 years considering the maintenance and replacement plans of the equipment and also supported by refrigeration equipment supplier and a third party. The change in accounting estimate is accounted for prospectively as of the date the change in estimate was made. The impact of this estimated change in 2006 was a reduction of depreciation expense by Ps. 127 recognized in 2006 consolidated results.

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The estimated useful lives of the Company's principal assets are as follows:

	<b>Years</b>
Buildings and construction	40-50
Machinery and equipment	12-20
Distribution equipment	10-12
Refrigeration equipment	5-7
Information technology equipment	3-4

**h) Other Assets:**

Other assets represent payments whose benefits will be received in future years and mainly consist of the following:

Agreements with customers for the right to sell and promote the Company's products during certain periods of time, which are considered monetary assets and amortized under two methods, in accordance with the terms of such agreements:

Actual volume method, which amortizes the proportion of the volume actually sold to the retailer over the volume target (approximately 85% of the agreements of FEMSA Cerveza are amortized on this basis); and

Straight-line method, which amortizes the asset over the life of the contract (the remaining 15% of the agreements of FEMSA Cerveza and 100% of the agreements of Coca-Cola FEMSA are amortized on this basis).

In addition, for agreements amortized based on the actual volume method, the Company periodically compares the amortization calculated based on the actual volume method against the amortization that would have resulted under the straight-line method and records a provision to the extent that the recorded amortization is less than what would have resulted under the straight-line method.

The amortization is recorded reducing net sales, which during the years ended December 31, 2006, 2005 and 2004, amounted to Ps. 1,360, Ps. 1,248 and Ps. 1,463, respectively.

Leasehold improvements, which are restated by applying inflation factors, are amortized using the straight-line method, over the shorter of the useful life of the assets or a term equivalent to the lease period.

**i) Intangible Assets:**

These assets represent payments whose benefits will be received in future years. The Company separates intangible assets between those with a finite useful life and those with an indefinite useful life, in accordance with the period over which the Company expects to receive the benefits.

Intangible assets with finite useful lives are amortized and mainly consist of:

Start-up expenses, which represent costs incurred prior to the opening of an Oxxo store, including rent, permits and licenses. Such amounts are restated applying inflation factors and are amortized on a straight-line basis in accordance with the terms of the lease contract; and

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Information technology and management systems costs incurred during the development stage. Such amounts are restated applying inflation factors and are amortized using the straight-line method over four years. Expenses that do not fulfill the requirements for capitalization are expensed as incurred.

Intangible assets with indefinite lives are not amortized and are subject to annual impairment test. These assets are recorded in the functional currency of the subsidiary in which the investment was made and were restated by applying inflation factors of the country of origin at the year-end exchange rate. The Company's intangible assets with indefinite lives mainly consist of:

Coca-Cola FEMSA's rights to produce and distribute Coca-Cola trademark products in the territories acquired. These rights are contained in agreements that are the standard contracts that The Coca-Cola Company enters into with bottlers outside the United States of America for the sale of concentrates for certain Coca-Cola trademark beverages;

Trademarks and distribution rights, recognized as a result of the acquisition of the 30% of FEMSA Cerveza (see Note 7) and payments made by FEMSA Cerveza in the acquisition of the previously granted franchise; and

Trademarks and goodwill recognized as a result of the acquisition of Kaiser (see Note 6).

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Goodwill represents the difference between the price paid and the fair value of the shares and/or net assets acquired that was not assigned directly to an intangible asset. Goodwill is recorded in the functional currency of the subsidiary in which the investment was made and is restated by applying inflation factors of the country of origin and the year-end exchange rate. Until December 31, 2004 goodwill was amortized using the straight-line method over a period of no more than 20 years.

### **j) Impairment of Long-Lived Assets and Goodwill:**

The Company reviews the carrying value of its long-lived assets for impairment and determines whether impairment exists, by comparing estimated discounted future cash flows to be generated by those assets with their carrying value.

For long-lived assets, such as property, plant and equipment, identifiable intangible assets and other assets, the Company tests for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or group of assets may not be recoverable through their expected future cash flows.

For goodwill, the Company tests for impairment on an annual basis and whenever certain circumstances indicate that the carrying amount of the reporting unit might exceed its implied fair value.

Impairment charges regarding long-lived assets and goodwill are recognized in other expenses.

### **k) Payments from The Coca-Cola Company:**

The Coca-Cola Company participates in certain advertising and promotional programs as well as in Coca-Cola FEMSA's refrigeration equipment investment program. The contributions received for advertising and promotional incentives are included as a reduction of selling expenses. The contributions received for the refrigeration equipment investment program are recorded as a reduction of the investment in refrigeration equipment. The contributions received were Ps. 1,164, Ps. 1,016 and Ps. 1,018 during the years ended December 31, 2006, 2005 and 2004, respectively.

### **l) Labor Liabilities:**

Labor liabilities include obligations for pension and retirement plans, seniority premiums, postretirement medical services and beginning in 2005 severance indemnity liabilities, all based on actuarial calculations by independent actuaries, using the projected unit credit method. Beginning January 1, 2005, revised Bulletin D-3 Labor Liabilities establishes that severance payments resulting from situations other than a restructuring should be charged to the income statement in accordance with actuarial calculations based on the Company's severance indemnity history of the last three to five years. Until December 31, 2004 such severance indemnities were charged to expenses on the date when a decision was taken.

Labor liabilities are considered to be non-monetary and are determined using long-term assumptions. The cost for the year of labor liabilities is charged to income from operations and unamortized prior service costs are recorded as expenses over the period during which the employees will receive the benefits of the plan.

Certain subsidiaries of the Company have established funds for the payment of pension benefits and postretirement medical services through irrevocable trusts with the employees named as beneficiaries.

Severance indemnities resulting from a restructuring program and associated with an ongoing benefit arrangement are charged to expenses on the date when a decision to retire personnel under a formal program or for specific causes is taken. These severance payments are included in other expenses. During the years ended December 31, 2006, 2005 and 2004, these payments amounted to Ps. 162, Ps. 126 and Ps. 165, respectively.

In 2006, Coca-Cola FEMSA implemented strategic restructuring programs in its commercial operations and recognized costs of Ps. 572, which are recorded in other expenses in the consolidated income statement. Such costs consist of Ps. 472 of severance payments associated with an ongoing benefit arrangement and Ps. 100 of other costs related to the restructuring programs. As of the end of 2006, Coca-Cola FEMSA has paid Ps. 201 and the remaining balance is expected to be paid during 2007.

**m) Revenue Recognition:**

Revenue is recognized in accordance with stated shipping terms, as follows:

For domestic sales, upon delivery to the customer and once the customer has taken ownership of the goods (FOB destination). Domestic revenues are defined as the sales generated by the Company for sales realized in the country where the subsidiaries operate. As of December 31, 2006, 2005 and 2004, domestic revenues represented approximately 97%, 96% and 97% of total consolidated revenues, respectively; and

For export sales, upon shipment of goods to customers (FOB shipping point), and transfer of ownership and risk of loss.

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Net sales reflect units delivered at list prices reduced by promotional allowances, discounts and the amortization of the agreements with customers to obtain the rights to sell and promote the products of the Company.

### **n) Operating Expenses:**

Administrative expenses include labor costs (salaries and other benefits) for employees not directly involved in the sale of the Company's products, professional service fees, depreciation of office facilities and amortization of capitalized information technology system implementation costs.

Selling expenses include:

Distribution: labor costs (salaries and other benefits), outbound freight costs, warehousing costs of finished products, breakage for returnable bottles in the distribution process, depreciation and maintenance of trucks and other distribution facilities and equipment. For the years ended December 31, 2006, 2005 and 2004, these distribution costs amounted to Ps. 9,190, Ps. 8,586 and Ps. 7,807, respectively;

Sales: labor costs (salaries and other benefits) and sales commissions paid to sales personnel; and

Marketing: labor costs (salaries and other benefits), promotions and advertising costs.

### **o) Income Tax, Tax on Assets and Employee Profit Sharing:**

Income tax and employee profit sharing are charged to results as they are incurred. Deferred income tax assets and liabilities are recognized for temporary differences resulting from comparing the book and tax values of assets and liabilities plus any future benefits from tax loss carryforwards. Deferred income tax assets are reduced by any benefits for which there is uncertainty as to their realizability. Deferred employee profit sharing is derived from temporary differences between the accounting result and income for employee profit sharing purposes and is recognized only when it can be reasonably assumed that the temporary differences will generate a liability or benefit, and there is no indication that circumstances will change in such a way that the liabilities will not be paid or benefits will not be realized.

The tax on assets paid that is expected to be recovered is recorded as a reduction of the deferred tax liability.

The balance of deferred taxes is comprised of monetary and non-monetary items, based on the temporary differences from which it is derived. Deferred taxes are classified as a long-term asset or liability, regardless of when the temporary differences are expected to reverse.

The deferred tax provision to be included in the income statement is determined by comparing the deferred tax balance at the end of the year to the balance at the beginning of the year, restated in currency of the current year, excluding from both balances any temporary differences that are recorded directly in stockholders' equity. The deferred taxes related to such temporary differences are recorded in the same stockholders' equity account.

FEMSA has authorization from the Secretaría de Hacienda y Crédito Público to prepare its income tax and tax on assets returns on a consolidated basis, which includes the proportional taxable income or loss of its Mexican subsidiaries. The provisions for income taxes of the foreign countries have been determined on the basis of the taxable income of each individual company. Prior to January 2005, for its Mexican subsidiaries, the proportional taxable income or loss was limited to 60% of the stockholders' ownership. Beginning in 2005, such limitation was eliminated.

### **p) Integral Result of Financing:**

The integral result of financing includes:

Interest: Interest income and expenses are recorded when earned or incurred, respectively;

Foreign Exchange Gains and Losses: Transactions in foreign currencies are recorded in local currencies using the exchange rate applicable on the date they occur. Assets and liabilities in foreign currencies are adjusted to the year-end exchange rate, recording the resulting foreign exchange gain or loss directly in the income statement, except for any foreign exchange gain or loss from financing obtained for the acquisition of foreign subsidiaries that are considered to be an economic hedge and the foreign exchange gain or loss from the intercompany financing foreign currency denominated balances that are considered to be of a long-term investment nature (see Note 3);

Gain or Loss on Monetary Position: Represents the result of the effects of inflation on monetary items. The gain or loss on monetary position is computed by applying inflation factors of the country of origin to the net monetary position at the beginning of each month, excluding the financing contracted for the acquisition of any foreign subsidiaries that are considered to be an economic hedge and the intercompany financing foreign currency denominated balances that are considered to be of a long-term investment nature (see Note 3). The gain or loss on monetary position of foreign subsidiaries is translated into Mexican pesos using the year-end exchange rate; and



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Market Value Gain or Loss on Ineffective Portion of Derivative Financial Instruments: Represents the net change in the fair value of, the ineffective portion of derivative financial instruments defined as hedges for accounting purposes and the net change in the fair value of embedded derivative financial instruments.

**q) Derivative Financial Instruments:**

On January 1, 2005, Bulletin C-10, Instrumentos Financieros Derivados y Operaciones de Cobertura (Derivative Financial Instruments and Hedging Activities) went into effect. Accordingly, the Company values and records all derivative financial instruments and hedging activities, including certain derivative financial instruments embedded in other contracts, in the balance sheet as either an asset or liability measured at fair value, considering quoted prices in recognized markets. If such instruments are not traded, fair value is determined by applying techniques based upon technical models supported by sufficient, reliable and verifiable data, recognized in the financial sector. Changes in the fair value of derivative financial instruments are recorded each year in net income or as a component of cumulative other comprehensive income, based on the type of hedging instrument and the ineffectiveness of the hedge.

The Company designates its financial instruments as hedging at the start of the hedging relationship, when transactions meet all hedging requirements. For cash flow hedges, the effective portion is recognized temporarily under comprehensive income within stockholders' equity, and subsequently reclassified to current earnings at the same time it is affected by the hedged item. When derivative financial instruments do not meet all of the standards requirements for hedging purposes, the ineffective portion is immediately recognized in net income.

The Company reviews all contracts entered into to identify embedded derivatives that should be segregated from the host contract for purposes of valuation and recording. When an embedded derivative is identified and the host contract has not been stated at fair value and adequate elements for its valuation exist, the embedded derivative is segregated from the host contract, stated at fair value and classified as trading or designated as a financial instrument for hedging. Initial valuation and changes in the fair value of the embedded derivatives at the closing of each period are recognized in net income.

Prior to the effective date of Bulletin C-10, the Company's derivative financial instruments entered into for hedging purposes were valued using the same valuation criteria applied to the hedged asset or liability, and their fair value were disclosed in the notes to the financial statements. Additionally, derivative financial instruments entered into for purposes other than hedging were valued and recorded at fair value. The difference between the derivative financial instrument's initial value and fair value was recorded in the income statement.

**r) Cumulative Other Comprehensive Loss:**

The cumulative balances of the components of majority other comprehensive loss are as follows:

	2006	2005
Cumulative result of holding non-monetary assets	Ps. (6,468)	Ps. (6,914)
Loss on cash flow hedges	(612)	(461)
Cumulative translation adjustment	(1,168)	(1,065)
Additional labor liability over unrecognized net transition obligation	(108)	(132)
	<b>Ps. (8,356)</b>	<b>Ps. (8,572)</b>

**s) Provisions:**

Provisions are recognized for obligations that result from a past event that will likely result in the use of economic resources and that can be reasonably estimated. Such provisions are recorded at net present values when the effect of the discount is significant.

**t) Issuances of Subsidiary Stock:**

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The Company recognizes issuances of a subsidiary's stock as a capital transaction, in which the difference between the book value of the shares issued and the amount contributed by the minority interest holder or a third party is recorded as additional paid-in capital.

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**Note 5. Acquisitions of Coca-Cola FEMSA Minority Interest**

On November 3, 2006, FEMSA indirectly acquired 148,000,000 serie D shares, which represent 8.02% of the total outstanding equity of Coca-Cola FEMSA for an aggregate amount of Ps. 4,627 paid in cash. This acquisition increased FEMSA's ownership stake in Coca-Cola FEMSA from 45.7% to 53.7% and its voting control from 53.6% to 63.0%. According to Mexican FRS this transaction occurs between shareholders and does not impact the net assets of the Company, and the payment in excess of the book value of the shares acquired is recorded in stockholders' equity as a reduction of additional paid-in capital in the amount of Ps. 1,551.

**Note 6. Acquisitions by FEMSA Cerveza.**

During 2006, FEMSA Cerveza made certain business acquisitions that were accounted for under the purchase method. The results of the operations acquired by FEMSA Cerveza have been included in the consolidated financial statements since the date of acquisition, as a result of which the 2006 consolidated income statement and balance sheet are not comparable with those of the prior year. The 2006 statement of changes in financial position presents the effects of the acquisitions and incorporation of such operations as a single line item within investing activities.

The Companies acquired by FEMSA Cerveza are:

- a) On January 13, 2006, FEMSA Cerveza indirectly acquired a controlling stake in Kaiser from Molson Coors Brewing Co. (Molson Coors) for Ps. 742 paid in cash, which represented 68% of the equity of Kaiser. The acquisition was accounted under the purchase method. FEMSA Cerveza assumed Kaiser's existing financial debt, which totaled approximately Ps. 654, and received certain indemnity provisions from Molson Coors for the potential payment of contingent liabilities and claims. Subsequent to the acquisition date, Kaiser paid Ps. 180 regarding such contingencies subject to the Molson Coors indemnifications and FEMSA Cerveza recorded a corresponding receivable for the amounts owed to them (see Note 8).

On December 18, 2006, FEMSA Cerveza, indirectly acquired Molson Coors' remaining 14.95% stake in Kaiser and paid Ps. 169 in cash. In accordance with Mexican FRS, this purchase was accounted for as an equity transaction as it took place between Kaiser's shareholders.

Additionally, FEMSA made an equity contribution of Ps. 2,156 on December 22, 2006 to Cervejarias Kaiser. Heineken NV, the other Kaiser shareholder, did not participate in this equity contribution and as a result its stake in Kaiser was diluted from 17.05% to 0.17%.

As of December 31, 2006, FEMSA Cerveza's stake in Kaiser's represents 99.83% of its outstanding equity. As a result of the step acquisition, FEMSA Cerveza identified and recorded intangible assets with indefinite lives consisting of trademarks of Ps. 524 and goodwill of Ps. 3,182 based on the preliminary purchase price allocation.

- b) In June 2006, FEMSA Cerveza acquired a beer distribution operation from a third-party distributors for an aggregate amount of Ps. 867. As a result of the acquisition, FEMSA Cerveza identified and recorded intangible assets with indefinite lives consisting beer distribution rights of Ps. 804 based on the preliminary purchase price allocation. No goodwill was recognized as of result of the acquisition.

**Note 7. Acquisition of FEMSA Cerveza Minority Interest.**

On August 31, 2004, the Company terminated the existing arrangements among affiliates of FEMSA and Interbrew S.A. (Interbrew), Labatt Brewing Company Limited and certain of their affiliates. As a result FEMSA indirectly owns 100% of FEMSA Cerveza; and Interbrew indirectly owns 100% of Labatt USA LLC and Latrobe Brewing Company LLC, its distribution subsidiaries in the United States of America.

The Company paid Interbrew Ps. 15,623 and incurred transaction costs of Ps. 237, which consisted of financial, advisory and legal fees, capitalized as adjustments to the purchase price. This transaction was financed with bridge loans which were paid through an equity offering completed on May 25, 2005.

The acquisition was accounted for under the purchase method and recorded trademarks and distribution rights as intangible assets with indefinite lives, for a total amount of Ps. 9,847. No goodwill was recognized as a result of the acquisition.



**Table of Contents****Note 8. Accounts Receivable.**

	2006	2005
Trade	<b>Ps. 6,084</b>	Ps. 4,437
Allowance for doubtful accounts	<b>(542)</b>	(482)
Notes receivable	<b>368</b>	356
Molson Coors (see Note 6 a)	<b>180</b>	
The Coca-Cola Company	<b>179</b>	422
Insurance claims	<b>60</b>	74
Travel advances to employees	<b>48</b>	34
Loans to employees	<b>43</b>	40
Guarantee deposits	<b>38</b>	239
Other	<b>516</b>	399
	<b>Ps. 6,974</b>	Ps. 5,519

The changes in the allowance for doubtful accounts are as follows:

	2006	2005	2004
Initial balance	<b>Ps. 482</b>	Ps. 467	Ps. 426
Provision for the year	<b>198</b>	188	210
Write-off of uncollectible accounts	<b>(119)</b>	(156)	(161)
Restatement of the initial balance	<b>(19)</b>	(17)	(8)
Ending balance	<b>Ps. 542</b>	Ps. 482	Ps. 467

**Note 9. Inventories.**

	2006	2005
Finished products	<b>Ps. 3,831</b>	Ps. 3,168
Raw materials	<b>3,432</b>	3,231
Advances to suppliers	<b>129</b>	70
Work in process	<b>277</b>	218
Spare parts	<b>583</b>	444
Advertising and promotional materials	<b>5</b>	8
Allowance for obsolescence	<b>(128)</b>	(49)
	<b>Ps. 8,129</b>	Ps. 7,090

**Note 10. Other Current Assets.**

	2006	2005
Advertising and promotional expenses	<b>Ps. 344</b>	Ps. 369
Restricted cash	<b>250</b>	84
Derivative financial instruments	<b>231</b>	207
Prepaid leases	<b>124</b>	83
Agreements with customers	<b>80</b>	87

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Advances to suppliers	<b>65</b>	55
Deferred promotional expenses	<b>38</b>	33
Prepaid insurance	<b>20</b>	18
Other	<b>14</b>	47
	<b>Ps. 1,166</b>	Ps. 983

The advertising and promotional expenses recorded in the income statements for the years ended December 31, 2006, 2005 and 2004 amounted to Ps. 4,572, Ps. 3,353 and Ps. 3,467, respectively.

**Table of Contents****Note 11. Investments in Shares.**

Company	Ownership	2006	2005
<b>FEMSA Cerveza:</b>			
Affiliated companies of FEMSA Cerveza <sup>(1)</sup>	Various	<b>Ps. 221</b>	Ps. 195
Río Blanco Trust (waste water treatment plant) <sup>(1)</sup>	19.12%	<b>74</b>	78
Other <sup>(2)</sup>	Various	<b>13</b>	14
<b>Coca-Cola FEMSA:</b>			
Industria Envasadora de Querétaro, S.A. de C.V. ( IEQSA <sup>(1)</sup> )	23.11%	<b>108</b>	156
KSP Participações, S.A. <sup>(1)</sup>	38.74%	<b>95</b>	92
Industria Mexicana de Reciclaje, S.A. de C.V. <sup>(1)</sup>	35.00%	<b>80</b>	86
Compañía de Servicios de Bebidas Refrescantes S.A. de C.V. ( Salesko <sup>(1)</sup> )	26.00%	<b>17</b>	21
Beta San Miguel, S.A. de C.V. ( Beta San Miguel <sup>(2)</sup> )	2.54%	<b>67</b>	67
Complejo Industrial Can, S.A. ( CICAN <sup>(1)</sup> )	48.10%	<b>38</b>	39
Other <sup>(2)</sup>	Various	<b>5</b>	8
Other investments <sup>(2)</sup>	Various	<b>50</b>	44
		<b>Ps. 768</b>	Ps. 800

Accounting method:

(1) Equity method.

(2) Restated acquisition cost (there is no readily determinable market value).

**Note 12. Property, Plant and Equipment.**

	2006	2005
Land	<b>Ps. 6,321</b>	Ps. 6,066
Buildings, machinery and equipment	<b>75,638</b>	69,137
Accumulated depreciation	<b>(37,938)</b>	(33,848)
Refrigeration equipment	<b>8,748</b>	7,736
Accumulated depreciation	<b>(6,646)</b>	(5,771)
Construction in progress	<b>2,413</b>	1,345
Long-lived assets stated at realizable value	<b>745</b>	765
Other long-lived assets	<b>109</b>	152
	<b>Ps. 49,390</b>	Ps. 45,582

The Company has identified certain long-lived assets that are not strategic to the current and future operations of the business and are available for sale, comprised of land, buildings and equipment for disposal, in accordance with an approved program for the disposal of certain investments. Such long-lived assets, which are not in use, and have been recorded at their estimated realizable value without exceeding their restated acquisition cost, as follows:

	2006	2005
FEMSA and others subsidiaries	<b>Ps. 296</b>	Ps. 306

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FEMSA Cerveza	<b>283</b>	260
Coca-Cola FEMSA	<b>166</b>	199
	<b>Ps. 745</b>	Ps. 765
Land	<b>Ps. 505</b>	Ps. 513
Buildings	<b>212</b>	224
Equipment	<b>28</b>	28
	<b>Ps. 745</b>	Ps. 765

As a result of selling certain long-lived assets, the Company recognized a gain of Ps. 19 and Ps. 26 for the years ended December 31, 2006 and 2004, respectively. In 2005 the result of selling long-lived assets was break-even.



**Table of Contents****Note 13. Intangible Assets.**

	2006	2005
<b>Unamortized intangible assets:</b>		
Coca-Cola FEMSA:		
Rights to produce and distribute Coca-Cola trademark products	<b>Ps. 39,399</b>	Ps. 39,001
FEMSA Cerveza:		
Trademarks and distribution rights	<b>10,897</b>	10,097
Goodwill	<b>3,182</b>	
Kaiser trademarks	<b>524</b>	
Other	<b>274</b>	226
Other unamortized intangible assets	<b>472</b>	472
<b>Amortized intangible assets:</b>		
Cost of systems implementation	<b>688</b>	783
Start-up expenses	<b>248</b>	243
Other	<b>149</b>	168
	<b>Ps. 55,833</b>	Ps. 50,990

The changes in the carrying amount of amortized intangible assets are as follows:

	Investments		Amortization		Estimated Amortization	
	Initial	Additions	Initial	For the Year	Total	Per Year
<b>2006:</b>						
Cost of systems implementation	<b>Ps. 1,522</b>	<b>Ps. 279</b>	<b>Ps. (739)</b>	<b>Ps. (374)</b>	<b>Ps. 688</b>	<b>Ps. 350</b>
Start-up expenses	<b>318</b>	<b>32</b>	<b>(75)</b>	<b>(27)</b>	<b>248</b>	<b>35</b>
<b>2005:</b>						
Cost of systems implementation	Ps. 1,140	Ps. 382	Ps. (431)	Ps. (308)	Ps. 783	
Start-up expenses	285	33	(52)	(23)	243	

**Note 14. Other Assets.**

	2006	2005
Leasehold improvements	<b>Ps. 3,508</b>	Ps. 2,823
Agreements with customers	<b>3,255</b>	3,243
Additional labor liabilities (see Note 17)	<b>1,226</b>	580
Long-term accounts receivable	<b>356</b>	407
Long-term licenses	<b>176</b>	119
Advertising and promotional expenses	<b>119</b>	67
Other	<b>812</b>	663
	<b>Ps. 9,452</b>	Ps. 7,902

**Table of Contents****Note 15. Balances and Transactions with Related Parties and Affiliated Companies.**

The consolidated balance sheets and income statements include the following balances and transactions with related parties and affiliated companies:

<b>Balances</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
Assets (accounts receivable)	<b>Ps. 442</b>	Ps. 671	
Liabilities (suppliers and other liabilities)	<b>2,124</b>	1,396	

<b>Transactions</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Income:</b>			
Export beer sales to Labatt USA <sup>(1)</sup>	<b>Ps.</b>	Ps.	Ps. 989
Interest income related to short-term bank deposits at BBVA Bancomer, S.A. <sup>(2) (4)</sup>			40
Sales of cans and aluminum lid to Promotora Mexicana de Embotelladores, S.A. de C.V.	<b>1,065</b>	966	974
Other revenues from affiliated companies of FEMSA Cerveza	<b>855</b>	821	816
Sales of non-carbonated soft-drinks to Salesko	<b>26</b>	19	
<b>Expenses:</b>			
Purchase of concentrate from The Coca-Cola Company	<b>9,298</b>	8,328	7,767
Purchase of baked goods and snacks from Grupo Industrial Bimbo, S.A. de C.V. <sup>(2)</sup>	<b>997</b>	916	813
Purchase of sugar, can and aluminum lid from Promotora Mexicana de Embotelladores, S.A. de C.V.	<b>833</b>	1,300	2,151
Purchase of canned products from IEQSA and CICAN	<b>785</b>	617	509
Purchase of sugar from Beta San Miguel	<b>516</b>	598	985
Interest expense paid to The Coca-Cola Company	<b>54</b>	12	15
Insurance premiums for policies with Grupo Nacional Provincial, S.A., Seguros Monterrey New York Life, S.A. and Fianzas Monterrey, S.A. <sup>(2) (4)</sup>	<b>39</b>	52	233
Purchase of plastic bottles from Embotelladora del Atlántico, S.A. (formerly Complejo Industrial Pet, S.A.) <sup>(2)</sup>	<b>32</b>	175	174
Purchases of crown caps from Tapón Corona, S.A. <sup>(3)</sup>		122	223
Interest expense related to long-term debt at BBVA Bancomer, S.A. <sup>(2) (4)</sup>			419
Management fees and technical assistance paid to Labatt <sup>(1)</sup>			91

(1) Labatt and Labatt USA were considered to be related parties until the acquisition by FEMSA of the remaining 30% interest of FEMSA Cerveza (see Note 7).

(2) One or more members of the board of directors or senior management are members of the board of directors or senior management of the counterparties to these transactions.

(3) In 2006, Tapón Corona is not considered to be related party.

(4) Since 2005, BBVA Bancomer, S.A. de C.V., Seguros Monterrey New York Life, S.A. and Fianzas Monterrey, S.A. are not considered to be related parties.

**Note 16. Balances and Transactions in Foreign Currencies.**

Assets, liabilities and transactions denominated in foreign currencies, other than the functional currencies of the reporting unit, translated into U.S. dollars are as follows:

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Applicable

Balances		Exchange Rate <sup>(1)</sup>	Short-Term	Long-Term	Total
<b>2006:</b>	<b>Assets</b>	<b>10.8755</b>	<b>\$ 107</b>	<b>\$ 16</b>	<b>\$ 123</b>
	<b>Liabilities</b>		<b>233</b>	<b>535</b>	<b>768</b>
2005:	Assets	10.7109	\$ 269	\$ 12	\$ 281
	Liabilities		369	545	914

(1) Mexican pesos per one U.S. dollar.

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<b>Transactions</b>	<b>2006</b>	2005	2004
Revenues	<b>\$ 387</b>	\$ 361	\$ 256
Expenses:			
Purchases of raw materials	<b>553</b>	468	411
Interest expense	<b>159</b>	139	116
Export expenses	<b>74</b>	65	29
Technical assistance fees	<b>11</b>	5	32
Other	<b>111</b>	84	102
	<b>\$ 908</b>	\$ 761	\$ 690

As of February 23, 2007, the issuance date of these consolidated financial statements, the exchange rate published by Banco de México was 11.0023 Mexican pesos per one U.S. dollar, and the foreign currency position was similar to that as of December 31, 2006.

**Note 17. Labor Liabilities.**

In December 2006, the Company approved to modify its pension and retirement plans effective in 2007. Through December 2006, the Company's pension and retirement plans provided for lifetime monthly payment as a complement to the pension payment received from the Mexican Social Security Institute (Instituto Mexicano del Seguro Social, IMSS). The modified pension and retirement plans, provide for one a lump-sum benefit payment, in addition to the pension benefits received from the IMSS which will supplement the beneficiary's earnings.

Additionally, FEMSA modified the long-term assumptions used in the actuarial calculations for its Mexican subsidiaries in 2006. The discount rate was reduced from 6.0% to 4.5% based on changes in the Company's revised estimate of current prices for settling its related obligations as a result of recent stability reflected by the Mexican economy. The expected salary increase was reduced from 2.0% to 1.5% based on changes in the estimated future compensation of its Mexican employees. The expected return on plan assets was reduced from 6% to 4.5% based on returns currently being earned by plan assets and the rates of return expected to be available for reinvestment in the future.

The net effect of the changes mentioned above was an increase in pension and retirement plan, seniority premium and severance indemnity liabilities of Ps. 768, Ps. 18 and Ps. 22, respectively. These changes were accounted as an unrecognized prior service costs and unrecognized actuarial net loss, which will be amortized over the expected service period of the Company's personnel.

**a) Assumptions:**

Actuarial calculations for pension and retirement plans, seniority premiums, postretirement medical services and severance indemnity liabilities, as well as the cost for the period, were determined in 2006 using the following long-term assumptions:

	<b>Real Rates</b>
Annual discount rate	4.5%
Salary increase	1.5%
Return on assets	4.5%
Measurement date: December 2006	

The basis for the determination of the long-term rate of return is supported by a historical analysis of average returns in real terms for the last 30 years of the Certificados de Tesorería del Gobierno Federal (Mexican Federal Government Treasury Certificates) for Mexican investments, Treasury Bonds of each country for other investments and the expected rates of return of long-term returns of the actual investments of the Company.

The annual growth rate for health care expenses is 2% in real terms, consistent with the historical average health care expense rate for the past 30 years and such rate is expected to remain consistent for the foreseeable future.



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Based on these assumptions, the expected benefits to be paid in the following years are as follows:

	<b>Pension and Retirement Plans</b>	<b>Seniority Premiums</b>	<b>Postretirement Medical Services</b>	<b>Severance Indemnities</b>
2007	Ps. 378	Ps. 11	Ps. 39	Ps. 106
2008	293	12	40	78
2009	280	13	41	70
2010	264	14	42	65
2011	316	17	44	59
2012 to 2016	1,325	155	325	195

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**Table of Contents****b) Balances of the Liabilities:**

	2006	2005
<b>Pension and retirement plans:</b>		
Vested benefit obligation	Ps. 2,130	Ps. 1,844
Non-vested benefit obligation	2,450	1,682
Accumulated benefit obligation	4,580	3,526
Excess of projected benefit obligation over accumulated benefit obligation	500	391
Projected benefit obligation	5,080	3,917
Pension plan funds at fair value	(2,612)	(2,197)
Unfunded projected benefit obligation	2,468	1,720
Unrecognized net transition obligation	(205)	(274)
Unrecognized prior service costs	(1,026)	
Unrecognized actuarial net gain (loss)	5	(141)
	1,242	1,305
Additional labor liability	896	351
Total	2,138	1,656
<b>Seniority premiums:</b>		
Vested benefit obligation	111	91
Non-vested benefit obligation	101	76
Accumulated benefit obligation	212	167
Excess of projected benefit obligation over accumulated benefit obligation	24	24
Unfunded projected benefit obligation	236	191
Unrecognized net transition obligation	(10)	(14)
Unrecognized actuarial net loss	(50)	(18)
	176	159
Additional labor liability	55	42
Total	231	201
<b>Postretirement medical services:</b>		
Vested benefit obligation	301	292
Non-vested benefit obligation	404	316
Accumulated benefit obligation	705	608
Medical services funds at fair value	(101)	(81)
Unfunded accumulated benefit obligation	604	527
Unrecognized postretirement net transition obligation	(41)	(57)
Unrecognized actuarial net loss	(322)	(280)
Total	241	190
<b>Severance indemnities:</b>		
Accumulated benefit obligation	503	460

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Excess of projected benefit obligation over accumulated benefit obligation	<b>39</b>	39
Projected benefit obligation	<b>542</b>	499
Unrecognized net transition obligation	<b>(453)</b>	(386)
Unrecognized actuarial net loss	<b>(33)</b>	
	<b>56</b>	113
Additional labor liability	<b>449</b>	396
<b>Total</b>	<b>505</b>	509
<b>Total labor liabilities</b>	<b>Ps. 3,115</b>	Ps. 2,556

The accumulated actuarial gains and losses were generated by the differences in the assumptions used for the actuarial calculations at the beginning of the year versus the actual behavior of those variables at the end of the current period.



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The projected benefit obligation in some subsidiaries was less than the accumulated benefit obligation reduced by the amount of the plan assets at fair value, resulting in an additional liability, which was recorded in other assets up to an amount of the unrecognized net transition obligation (see Note 14) and the difference was recorded in other comprehensive loss.

**c) Trust Assets:**

Trust assets consist of fixed and variable return financial instruments, at market value. The trust assets are invested as follows:

	2006	2005
<b>Fixed Return:</b>		
Traded securities	25%	17%
Bank instruments	20%	16%
Federal government instruments	31%	30%
<b>Variable Return:</b>		
Publicly traded	24%	37%
	100%	100%

The Company has a policy of maintaining at least 30% of the trust assets in Mexican Federal Government instruments. Objective portfolio guidelines have been established for the remaining percentage, and investment decisions are made to comply with those guidelines to the extent that market conditions and available funds allow. The composition of the portfolio is consistent with those of other large multi-national companies that manage long-term funds.

During 2006, the contributions to the pension plan and postretirement medical services trust assets amounted to Ps. 270, and the Company estimates that the contributions during 2007 will reach approximately Ps. 470.

The amounts and types of securities of the Company and related parties included in trust assets are as follows:

	2006	2005
<b>Debt:</b>		
Grupo Industrial Bimbo, S.A. de C.V. <sup>(1)</sup>	Ps. 10	Ps. 11
Coca-Cola FEMSA		46
FEMSA		23
<b>Capital:</b>		
FEMSA	185	302

- (1) One or more members of the board of directors or senior management are members of the board of directors or senior management of this Company.

**Table of Contents****d) Cost for the Year:**

	2006	2005	2004
<b>Pension and retirement plans:</b>			
Service cost	<b>Ps. 130</b>	Ps. 115	Ps. 115
Interest cost	<b>220</b>	205	206
Expected return on trust assets	<b>(131)</b>	(119)	(113)
Amortization of unrecognized transition obligation	<b>53</b>	52	25
Amortization of net actuarial loss	<b>5</b>	1	
	<b>277</b>	254	233
<b>Seniority premiums:</b>			
Service cost	<b>23</b>	22	21
Interest cost	<b>11</b>	10	10
Amortization of unrecognized transition obligation	<b>2</b>	2	1
Amortization of net actuarial loss	<b>1</b>		
	<b>37</b>	34	32
<b>Postretirement medical services:</b>			
Service cost	<b>20</b>	19	16
Interest cost	<b>34</b>	33	29
Expected return on trust assets	<b>(3)</b>	(3)	(2)
Amortization of unrecognized transition obligation	<b>5</b>	5	13
Amortization of net actuarial loss	<b>9</b>	11	
	<b>65</b>	65	56
<b>Severance indemnities:</b>			
Service cost	<b>77</b>	58	
Interest cost	<b>31</b>	28	
Amortization of unrecognized transition obligation	<b>34</b>	29	
	<b>142</b>	115	
	<b>Ps. 521</b>	Ps. 468	Ps. 321

**Table of Contents**e) **Changes in the Balance of the Obligations:**

	2006	2005
<b>Pension and retirement plans:</b>		
Initial balance	<b>Ps. 3,917</b>	Ps. 3,653
Service cost	<b>130</b>	115
Interest cost	<b>220</b>	205
Curtailement	<b>(23)</b>	
Amendments	<b>999</b>	
Actuarial loss	<b>32</b>	219
Benefits paid	<b>(195)</b>	(275)
Ending balance	<b>5,080</b>	3,917
<b>Seniority premiums:</b>		
Initial balance	<b>191</b>	179
Service cost	<b>23</b>	22
Interest cost	<b>11</b>	10
Actuarial loss	<b>44</b>	8
Benefits paid	<b>(33)</b>	(28)
Ending balance	<b>236</b>	191
<b>Postretirement medical services:</b>		
Initial balance	<b>608</b>	566
Service cost	<b>20</b>	19
Interest cost	<b>34</b>	33
Actuarial loss	<b>86</b>	9
Benefits paid	<b>(43)</b>	(19)
Ending balance	<b>705</b>	608
<b>Severance indemnities:</b>		
Initial balance	<b>499</b>	520
Kaiser acquisition	<b>27</b>	
Service cost	<b>77</b>	58
Interest cost	<b>31</b>	28
Actuarial loss	<b>31</b>	
Benefits paid	<b>(123)</b>	(107)
Ending balance	<b>542</b>	499

**Table of Contents****f) Changes in the Balance of the Trust Assets:**

	2006	2005
<b>Pension and retirement plans:</b>		
Initial balance	<b>Ps. 2,197</b>	Ps. 1,982
Actual return on trust assets in real terms	<b>363</b>	247
Contributions	<b>208</b>	150
Benefits paid	<b>(156)</b>	(182)
Ending balance	<b>2,612</b>	2,197
<b>Postretirement medical services:</b>		
Initial balance	<b>81</b>	65
Actual return on trust assets in real terms	<b>1</b>	7
Contributions	<b>62</b>	28
Benefits paid	<b>(43)</b>	(19)
Ending balance	<b>101</b>	81

**g) Variation in Health Care Assumptions:**

The following table presents the impact to the postretirement medical service obligations and the expenses recorded in the income statement with a variation of 1% in the assumed health care cost trend rates.

	<b>Impact of changes:</b>	
	+ 1%	- 1%
Postretirement medical services obligation	Ps. 90	Ps. (119)
Cost for the year	18	(4)

**Note 18. Bonus Program.**

The bonus program for executives is based on complying with certain goals established annually by management, which include quantitative and qualitative objectives and special projects.

The quantitative objectives represent approximately 50% of the bonus and are based on the Economic Value Added (EVA) methodology. The objective established for the executives at each entity is based on a combination of the EVA per entity and the EVA generated by the Company, calculated at approximately 70% and 30%, respectively. The qualitative objectives and special projects represent the remaining 50% of the annual bonus and are based on the critical success factors established at the beginning of the year for each executive.

In addition, the Company provides a share compensation plan to certain key executives, consisting of an annual cash bonus to purchase FEMSA shares or options, based on the executive's responsibility in the organization, their business EVA result achieved, and their individual performance. The acquired shares or options are deposited in a trust, and the executives may access them one year after they are vested at 20% per year. 50% of Coca-Cola FEMSA's annual executive bonus is to be used to purchase FEMSA shares or options and the remaining 50% to purchase Coca-Cola FEMSA shares or options.

The incentive plan target is expressed in months of salary, and the final amount payable is computed based on a percentage of compliance with the goals established every year. The bonuses are recorded in income from operations and are paid in cash the following year. During the years ended December 31, 2006, 2005 and 2004, the bonus expense recorded amounted to Ps. 862, Ps. 664 and Ps. 649, respectively.

All shares held by the trusts are considered outstanding for earnings per share purposes and dividends on shares held by the trusts are charged to retained earnings.



**Table of Contents****Note 19. Bank Loans and Notes Payable.**

The following table presents short-term debt consisted principally of revolving bank loans as well as their weighted average rates:

	% Interest		% Interest	
	Rate	2006	Rate	2005
Mexican pesos	7.6%	Ps. 406	4.4%	Ps. 47
U.S. dollars	5.9%	1,791	4.7%	5
Argentine pesos	10.6%	527	9.4%	247
Venezuelan bolivars	9.6%	422	12.1%	463
Brazilian reals	13.9%	102		
Japanese yen	2.9%	242		
		<b>Ps. 3,490</b>		<b>Ps. 762</b>

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The following table presents long-term bank loans and notes payable, as well as their weighted average rates and derivative financial instruments contracted by the Company:

	% Interest		% Interest	
	Rate	2006	Rate	2005
<b>Fixed interest rate:</b>				
<b>U.S. dollars:</b>				
Yankee bonds	7.3%	Ps. 3,233	7.9%	Ps. 5,576
Bank loans	5.3%	642	3.4%	263
Capital leases			5.6%	118
<b>Mexican pesos:</b>				
Bank loans	9.7%	4,136	9.6%	4,304
Notes	10.2%	1,500	10.2%	1,561
Units of investment (UDI)			8.7%	1,483
<b>Japanese yen:</b>				
Bank loans	5.8%	151		
<b>Variable interest rate:</b>				
<b>U.S. dollars:</b>				
Bank loans	5.7%	2,660	4.8%	2,470
Capital leases	8.7%	9	6.9%	53
<b>Mexican pesos:</b>				
Bank loans	7.6%	15,971	9.0%	10,602
Notes	8.2%	8,156	9.7%	8,486
<b>Colombian pesos:</b>				
Notes	9.3%	166	8.7%	401
<b>Brazilian reals:</b>				
Bank loans	9.3%	67		
<b>Guatemalan quetzals:</b>				
Bank loans			6.5%	26
<b>Long-Term Debt</b>		<b>36,691</b>		<b>35,343</b>
Current maturities of long-term debt		(2,440)		(4,401)
		<b>Ps. 34,251</b>		<b>Ps. 30,942</b>

	% Interest		% Interest	
	Rate <sup>(1)</sup>	2006	Rate <sup>(1)</sup>	2005
<b>Hedging Derivative Financial Instruments</b>				
<b>Interest rate swaps variable to fixed:</b>				
<b>Mexican pesos:</b>				
<b>Bank loans:</b>				
		<b>Ps. 11,835</b>		<b>Ps. 8,399</b>
Interest pay rate	9.8%		10.3%	
Interest receive rate	7.4%		9.1%	
<b>Notes:</b>				
		<b>8,156</b>		<b>8,486</b>
Interest pay rate	9.2%		9.2%	
Interest receive rate	8.0%		9.7%	
<b>Cross currency swaps:</b>				
Bank loans from U.S. dollars to Mexican pesos:				
				<b>1,561</b>
Interest pay rate			11.1%	
Interest receive rate			4.8%	
Bank loans from Japanese yen to Brazilian reals:				
		<b>393</b>		
Interest pay rate	13.9%			
Interest receive rate	4.0%			

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(1) Weighted average rate.

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Maturities of long-term debt as of December 31, 2006 are as follows:

Current maturities of long-term debt	Ps. 2,440
2008	5,854
2009	5,436
2010	4,902
2011	4,138
2012 and thereafter	13,921
	Ps. 36,691

The Company has financing from different institutions with different restrictions and covenants, which mainly consist of maximum levels of leverage and capitalization as well as minimum consolidated net worth and debt and interest coverage ratios. As of the date of these consolidated financial statements, the Company was in compliance with all restrictions and covenants contained in its financing agreements.

**Note 20. Fair Value of Financial Instruments.****a) Long-Term Debt:**

The fair value of long-term bank loans and syndicated loans is based on the discounted value of contractual cash flows, in which the discount rate is estimated using rates currently offered for debt of similar amounts and maturities. The fair value of long-term notes is based on quoted market prices. The fair value is estimated as of the date.

	<b>2006</b>	2005
Carrying value	<b>Ps. 36,691</b>	Ps. 35,343
Fair value	<b>37,138</b>	35,842

**b) Interest Rate Swaps:**

The Company uses interest rate swaps to manage the interest rate risk associated with its borrowings, pursuant to which it pays amounts based on a fixed rate and receives amounts based on a floating rate. The fair value is estimated based on quoted market prices to terminate the contracts at the date of the most reporting date. The changes in the fair value were recorded in cumulative other comprehensive loss.

At December 31, 2006, the Company has the following outstanding interest rate swap agreements:

Maturity	Notional	Fair Value
Date	Amount	Liability
2007	Ps. 4,250	Ps. (36)
2008	5,000	(87)
2009	2,405	(147)
2010	3,513	(260)
2011	2,413	(152)
2012	1,500	(155)
2013	2,000	(52)

The net effect of expired contracts is included in interest expense and amounted to Ps. 322, Ps. 28 and Ps. 158 for the years ended December 31, 2006, 2005 and 2004, respectively.

A portion of certain interest rate swaps do not meet the hedging criteria for accounting purposes; consequently changes in the estimated fair value were recorded in the result of financing as a loss in the market value on ineffective portion of derivative financial instruments, as part of the integral result of financing.

The net effect of these contracts as of the issuance of the financial statements was a loss of Ps. 36. As of December 31, 2005, there are no ineffective amounts regarding, the Company's interest rate swaps.

**c) Forward Agreements to Purchase Foreign Currency:**

The Company entered into forward agreements to reduce its exposure to the risk of exchange rate fluctuations between the Mexican pesos and the euro for the purchase of equipment. The fair value is estimated based on quoted market prices to terminate the contracts at the date of the reporting date. The changes in the fair value were recorded in cumulative other comprehensive loss. As of December 31, 2006 the notional amount of these contracts amounted to 2 million with a fair value asset of Ps. 2. The contracts expire in January 2007.

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The net effect of the Company's expired foreign exchange contracts are losses of Ps. 2, Ps. 9 and Ps. 18 for the years ended December 31, 2006, 2005 and in 2004; such effects were recorded as foreign exchange loss in the integral result of financing.

In connection with the bridge loans incurred regarding the acquisition of FEMSA Cerveza's minority interest, the Company entered into forward contracts to buy U.S. dollars. This transaction generated a foreign exchange loss of Ps. 162 recorded in the income statement for the year ended December 31, 2005. These forward contracts were terminated in 2005 in conjunction with the payment of the bridge loans.

As of December 31, 2006, certain of the Company's forward contracts to buy U.S. dollars and other currencies do not meet the hedging criteria for accounting purposes; consequently changes in the fair value were recorded in the integral result of financing as a market value gain or loss on ineffective portion of derivative financial instruments as part of the integral result of financing.

The notional amount of such contracts that mature in 2007 is Ps. 1,144 with fair value asset of Ps. 41. The net effect of expired contracts amounting to Ps. 22 that did not meet the hedging criteria for accounting purposes is included as a market value loss on the ineffective portion of derivative financial instruments. As of December 31, 2005, there are no effects of forwards agreements to purchase foreign currency.

### **d) Cross Currency Swaps:**

The Company enters into cross currency swaps to reduce its exposure to the risk of exchange rate and interest fluctuations associated with its borrowings denominated in U.S. dollars and other foreign currencies. The fair value is estimated based on the quoted market exchange rates and interest rates to terminate the contracts at the date of the reporting date. The changes in the fair value were recorded in cumulative other comprehensive loss.

As of December 31, 2006, the Company has cross currency swap agreements outstanding with a fair value liability of Ps. 18 and a notional amount of Ps. 393. Those contracts mature in 2007.

The net effect of expired contracts included in interest expenses as part of the integral result of financing amounted to Ps. 70 and Ps. 130, for the years ended December 31, 2006 and 2005, respectively.

Certain cross currency swaps instruments did not meet the hedging criteria for accounting purposes; consequently changes in the estimated fair value are recorded as a loss in the market value on ineffective portion of derivative financial instruments as part of the integral result of financing.

Those contracts with a notional amount of Ps. 2,843 expire in December 2011 and the net effect changes in the fair value amounted Ps. 47 of a loss recorded in the market value on ineffective portion of derivative financial instruments.

The net effect of expired contracts that did not meet the hedging criteria for accounting purposes is recorded as a market value loss on ineffective portion of derivative financial instruments and amounted to Ps. 3 and Ps. 226 for the year ended December 31, 2006 and 2005, respectively.

### **e) Commodity Price Contracts:**

The Company enters into various commodity price contracts to reduce its exposure to the risk of certain raw material costs. The fair value is estimated based on quoted market prices to terminate the contracts at the reporting date. The changes in the fair value were recorded in cumulative other comprehensive loss.

As of December 31, 2006, the Company has commodity price contracts with maturity dates ending in 2008, with a notional amount of Ps. 1,029 and had recorded a fair value liability of Ps. 75.

As of the end of 2006 and 2005 the net effect of expired commodity price contracts were losses of Ps. 104 and Ps. 2, respectively, and were recorded as part of operating income offsetting the related raw material cost.

**Table of Contents****f) Embedded Derivative Financial Instruments:**

The Company has determined that its leasing contracts denominated in U.S. dollars host embedded derivative financial instruments. The fair value is estimated based on quoted market prices to terminate the contracts at the reporting date. The changes in the fair value were recorded in the integral result of financing as market value on ineffective portion of derivative financial instruments.

As of December 31, 2006 and 2005 the Company has recognized the fair value of such instruments as a market value assets of Ps. 67 and Ps. 124, respectively.

**Note 21. Minority Interest in Consolidated Subsidiaries.**

	2006	2005
Coca-Cola FEMSA	Ps. 19,849	Ps. 20,412
FEMSA Cerveza	159	50
	<b>Ps. 20,008</b>	Ps. 20,462

**Note 22. Stockholders Equity.**

As of December 31, 2006, the capital stock of FEMSA was comprised of 5,963,710,450 common shares, without par value and with no foreign ownership restrictions. Fixed capital amounts to Ps. 300 (nominal value) and the variable capital may not exceed 10 times the minimum fixed capital stock.

The characteristics of the common shares are as follows:

Series B shares, with unlimited voting rights, which at all times must represent a minimum of 51% of total capital stock;

Series L shares, with limited voting rights, which may represent up to 25% of total capital stock; and

Series D shares, with limited voting rights, which individually or jointly with series L shares may represent up to 49% of total capital stock.

The Series D shares are comprised as follows:

Subseries D-L shares may represent up to 25% of the series D shares;

Subseries D-B shares may comprise the remainder of outstanding series D shares; and

The non-cumulative premium dividend to be paid to series D stockholders will be 125% of any dividend paid to series B stockholders. The Series B and D shares are linked together in related units as follows:

B units each of which represents five series B shares and which are traded on the BMV;

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BD units each of which represents one series B share, two subseries D-B shares and two subseries D-L shares, and which are traded both on the BMV and the NYSE; and

The related units will cease to be linked together on May 2008, after a period of 10 years from the date of the first issue. Subseries D-B shares will be converted into series B shares, and subseries D-L shares will be converted into series L shares.  
As of December 31, 2006, FEMSA's capital stock is comprised as follows:

Units	B Units	BD Units	Total
Units	472,349,500	720,392,590	1,192,742,090
Shares:			
Series B	2,361,747,500	720,392,590	3,082,140,090
Series D		2,881,570,360	2,881,570,360
Subseries D-B		1,440,785,180	1,440,785,180
Subseries D-L		1,440,785,180	1,440,785,180
<b>Total shares</b>	<b>2,361,747,500</b>	<b>3,601,962,950</b>	<b>5,963,710,450</b>

On May 25, 2005, the Company completed an equity offering, obtaining net proceeds of Ps. 8,155, which were used to repay the bridge loans incurred in connection with the acquisition of a 30% equity interest in FEMSA Cerveza and to repay other indebtedness. As a result of the equity offering in 2005, the Company's capital stock increased by 666,400,000 shares.

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The restatement of stockholders' equity for inflation is allocated to each of the various stockholders' equity accounts, as follows:

	Historical		Restated
	Value	Restatement	Value
Capital stock	Ps. 2,982	Ps. 2,172	Ps. 5,154
Additional paid-in capital	13,269	6,543	19,812
Retained earnings from prior years	29,178	1,810	30,988
Net income	6,465	157	6,622

The net income of the Company is subject to the legal requirement that 5% thereof be transferred to a legal reserve until such reserve equals 20% of capital stock at nominal value. This reserve may not be distributed to stockholders during the existence of the Company, except as a stock dividend. As of December 31, 2006, this reserve for FEMSA amounted to Ps. 596 (nominal value).

Retained earnings and other reserves distributed as dividends, as well as the effects derived from capital reductions, are subject to income tax at the rate in effect, except for the restated stockholder contributions and distributions made from consolidated taxable income, denominated Cuenta de Utilidad Fiscal Neta ( CUFIN ) or from reinvested consolidated taxable income, denominated Cuenta de Utilidad Fiscal Neta Reinvertida ( CUFINRE ).

Dividends paid in excess of CUFIN and CUFINRE are subject to income tax at a grossed-up rate based on the current statutory rate. In 2003, this tax may be credited against the income tax of the year in which the dividends are paid and in the following two years against the income tax and estimated tax payments. As of December 31, 2006, FEMSA's balances of CUFIN and CUFINRE amounted to Ps. 30,501 and Ps. 1,114, respectively, and the deferred tax payments were Ps. 86.

At an ordinary stockholder meeting of FEMSA held on March 10, 2006, the stockholders approved a dividend of 0.147514 Mexican pesos (nominal value) per series B share and 0.184393 Mexican pesos (nominal value) per series D share that were paid in June 2006. Additionally, the stockholders approved a maximum of Ps. 3,000 for a stock repurchase program.

At an ordinary stockholder meeting of Coca-Cola FEMSA held on March 8, 2006, the stockholders approved a dividend of Ps. 716 that were paid in June 2006. The corresponding payment to the minority interest was Ps. 389.

**Note 23. Net Majority Income per Share.**

This represents the net majority income corresponding to each share of the Company's capital stock, computed on the basis of the weighted average number of shares outstanding during the period. Additionally, the net income distribution according to the dividend rights of each share series is presented.

The following presents the computed weighted average number of shares and the distribution of income per share series as of December 31, 2006, 2005 and 2004:

	Millions of Shares			
	Series B		Series D	
	Number	Weighted Average	Number	Weighted Average
Shares outstanding at December 31, 2004	2,737.74	2,739.17	2,559.57	2,561.00
Increase in capital stock on May 25, 2005	344.40	205.78	322.00	192.38
Shares outstanding at December 31, 2005	3,082.14	2,944.95	2,881.57	2,753.38
Shares outstanding at December 31, 2006	3,082.14	3,082.14	2,881.57	2,881.57
Dividend rights	1.00		1.25	
Allocation of earnings	46.11%		53.89%	

**Note 24. Tax System.**

**a) Income Tax:**

Income tax is computed on taxable income, which differs from accounting income principally due to the treatment of the integral result of financing, the cost of labor liabilities, depreciation and other accounting provisions. The tax loss may be carried forward and applied against future taxable income as shown below.

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The income tax rates applicable in 2006 in the countries where the Company operates and the years in which tax loss carryforwards may be applied are as follows:

	Statutory Tax Rate	Expiration (Years)
Mexico	29.0%	10
Guatemala	31.0%	N/A
Nicaragua	30.0%	3
Costa Rica	30.0%	3
Panama	30.0%	5
Colombia	38.5%	5-8
Venezuela	34.0%	3
Brazil	34.0%	Indefinite
Argentina	35.0%	5

The statutory income tax rate in Mexico for the years ended December 31, 2006, 2005 and 2004 was 29%, 30% and 33%, respectively.

Beginning January 1, 2005, an amendment to the income tax law in Mexico was effective and the principal changes were as follows:

The statutory income tax rate decreased from 30% in 2005 to 29% in 2006, and it will be reduced to 28% in 2007 and thereafter;

The tax deduction for inventories is made through cost of sales, and the inventory balance as of December 31, 2004 will be taxable during the next 4 to 12 years, based on specific criteria within the tax law;

Paid employee profit sharing is deductible for income tax purposes; and

The 60% limit of the stockholders' participation in the taxable income or loss of Mexican subsidiaries was eliminated for tax consolidation purposes.

In Colombia, the tax losses generated before December 31, 2002, may be carried forward five years and those generated after January 1, 2003, may be carried forward eight years. Both are limited to 25% of taxable income of each year. Additionally, the statutory tax rate of Colombia decreases from 38.5% in 2006 to 34% in 2007 and 33% in 2008, and the tax impose to dividends of 5% was eliminated in 2006.

In Brazil, tax losses may be carried forward for an indefinite period but cannot be restated and are limited to 30% of the taxable income of each year.

**b) Tax on Assets:**

Through 2006, the Mexican tax on assets was computed at an annual rate of 1.8% based on the average of certain assets at tax restated value less certain liabilities. Since January 1, 2007 the tax on assets changed from 1.8% to 1.25% and also the deduction of liabilities was eliminated in order to determine the tax to be paid. The tax on assets is paid only to the extent that it exceeds the income tax of the year. If in any year a tax on assets payment is required, this amount can be credited against the excess of income taxes future payments over the tax on assets in each of the preceding three years. Additionally, this payment may be restated and credited against the excess of income taxes over asset taxes for the following 10 years.

The operations in Guatemala, Nicaragua, Colombia and Argentina are also subject to a minimum tax, which is based primarily on a percentage of assets. Any payments are recoverable in future years, under certain conditions.



**c) Employee Profit Sharing:**

Employee profit sharing is applicable to Mexico and Venezuela. In Mexico, employee profit sharing is computed at the rate of 10% of the individual taxable income, except that depreciation of historical rather than restated values is used, foreign exchange gains and losses are not included until the asset is disposed of or the liability is due, and other effects of inflation are also excluded. In Venezuela, employee profit sharing is computed at a rate equivalent to 15% of after tax earnings.

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**Table of Contents****d) Deferred Income Tax:**

The temporary differences that generated deferred income tax liabilities (assets) are as follows:

<b>Deferred Income Taxes</b>	<b>2006</b>	<b>2005</b>
Allowance for doubtful accounts	Ps. (104)	Ps. (145)
Inventories	530	850
Prepaid expenses	126	118
Property, plant and equipment	4,955	4,771
Investments in shares	(9)	(11)
Intangible and other assets	(784)	(750)
Labor liabilities	(477)	(512)
Recoverable tax on assets	(48)	(83)
Tax loss carryforwards	(3,342)	(1,165)
Valuation allowance	2,664	515
Derivative financial instruments	(247)	(256)
Loss contingencies	(440)	(709)
Temporary non deductible provision	(729)	(440)
Employee profit sharing	(145)	(142)
Other reserves	157	102
Deferred income tax, net	2,107	2,143
Deferred income tax asset	1,727	1,390
Deferred income tax liability	Ps. 3,834	Ps. 3,533

The changes in the balance of the deferred income tax, net are as follows:

	<b>2006</b>	<b>2005</b>
Initial balance	Ps. 2,143	Ps. 2,802
Loss on monetary position	(27)	(14)
Tax provision for the year	34	(132)
Change in the statutory income tax rate	(16)	(10)
Effects in stockholders equity:		
Additional labor liability over unrecognized net transition obligation	10	(60)
Derivative financial instruments	(10)	(256)
Result of holding non-monetary assets	(27)	(187)
Ending balance	Ps. 2,107	Ps. 2,143

There are no significant non-recurring temporary differences between the accounting income for the year and the bases used for Mexican employee profit sharing. As a result, the Company has not recorded a provision for deferred employee profit sharing.

**e) Provision for the Year:**

	<b>2006</b>	<b>2005</b>	<b>2004</b>
Current income tax	Ps. 4,226	Ps. 4,428	Ps. 4,593
Tax on assets	52	14	74
Deferred income tax	34	(132)	(407)

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Change in the statutory income tax rate	(16)	(10)	(647)
Benefit from favorable tax ruling			(1,410)
Income tax	<b>4,296</b>	4,300	2,203
Employee profit sharing	<b>510</b>	566	446
	<b>Ps. 4,806</b>	Ps. 4,866	Ps. 2,649

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**Table of Contents****f) Tax Loss Carryforwards and Recoverable Tax on Assets:**

The subsidiaries from Mexico, Panama, Colombia, Venezuela and Brazil have tax loss carryforwards and/or recoverable tax on assets. The expiration dates of such amounts are as follows:

Year	Tax Loss	Recoverable
	Carryforwards	Tax on Assets
2007	Ps. 1	Ps.
2008	1	
2009	35	
2010	60	8
2011	16	2
2012	35	12
2013	144	12
2014	233	22
2015	142	
2016 and thereafter		
No expiration (Brazil, see Note 24 a)	9,265	
	Ps. 9,932	Ps. 56

Due to the uncertainty of the realization of tax loss carryforwards, Ps. 7,833 has been excluded from the deferred income tax asset associated with such carryforwards. The changes in the valuation allowance which reduce the related deferred tax asset are as follows:

	2006	2005
Initial balance	Ps. 515	Ps. 550
Kaiser acquisition	2,490	
Provision of the year		122
Cancellation of provision	(325)	(128)
Restatement of the initial balance	(16)	(29)
Ending balance	Ps. 2,664	Ps. 515

**g) Reconciliation of Mexican Statutory Income Tax Rate to Consolidated Effective Income Tax Rate:**

	2006	2005	2004
Mexican statutory income tax rate	29.0%	30.0%	33.0%
Difference between book and tax inflationary effects	(0.1)%	0.6%	(3.1)%
Non-deductible expenses	3.3%	1.9%	4.8%
Change in inventories tax deduction		(2.1)%	
Change in Mexican income tax rate	0.1%		(5.8)%
Employee profit sharing	(1.0)%	(1.1)%	
Non-taxable income	(1.5)%	(0.1)%	
Benefit from favorable tax ruling			(12.4)%
Other	0.9%	2.8%	0.8%
Consolidated effective income tax rate	30.7%	32.0%	17.3%



**Table of Contents****Note 25. Contingencies and Commitments.****a) Contingencies Recorded in the Balance Sheet:**

The Company has various loss contingencies, and reserves have been recorded in those cases where the Company believes an unfavorable resolution is probable. Most of these loss contingencies were recorded as a result of the Coca-Cola FEMSA territories acquisition in the Latin American and Kaiser acquisition. The following table presents the nature and amount of the loss contingencies recorded as of December 31, 2006:

	<b>Total</b>
Tax	Ps. 1,549
Legal	219
Labor	512
 Total	 Ps. 2,280

**b) Unsettled Lawsuits:**

The Company has entered into legal proceedings with its labor unions, tax authorities and other parties that primarily involve Coca-Cola FEMSA and FEMSA Cerveza. These proceedings have resulted in the ordinary course of business and are common to the industry in which the Company operates. The aggregate amount of these proceedings is \$86. Those contingencies were classified by legal counsel as less than probable but more than remote of being settled against the Company. However the Company believes that the ultimate resolution of such legal proceedings will not have a material adverse effect on its consolidated financial position or result of operations.

In recent years in its Mexican, Costa Rican and Brazilian territories, Coca-Cola FEMSA and FEMSA Cerveza have been requested to present certain information regarding possible monopolistic practices. These requests are commonly generated in the ordinary course of business in the beer and soft drink industries where those subsidiaries operate.

In 2001, a labor union and several individuals from the Republic of Colombia filed a lawsuit in the U.S. District Court for the Southern Division of Florida against certain Colombian subsidiaries and The Coca-Cola Company. In the complaint, the plaintiffs alleged that the subsidiaries engaged in wrongful acts against the labor union and its members in Colombia for the amount of \$500. The Company has filed a motion to dismiss the complaint. On September 29, 2006 the Court entered a consolidated omnibus order dismissing the case for lack of subject matter jurisdiction and conclusively ruled that the Court did not have subject matter jurisdiction over any of the labor union and its member actions, and thus all of the claims against the Company were effectively dismissed. However, the plaintiffs have appealed this ruling.

**c) Collateralize Contingencies:**

As is customary in Brazil, the Company has been requested by the tax authorities to collateralize tax contingencies currently in litigation amounting to Ps. 1,415 by pledging fixed assets and entering into available lines of credit which cover such contingencies.

**d) Commitments:**

As of December 31, 2006, the Company has capital and operating lease commitments for the leasing of production machinery and equipment, distribution equipment, computer equipment and land for FEMSA Comercio's operations.

The contractual maturities of the lease commitments by currency, expressed in Mexican pesos as of December 31, 2006, are as follows:

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	<b>Mexican Pesos</b>	<b>U.S. Dollars</b>	<b>Others</b>
2007	Ps. 1,037	Ps. 700	Ps. 71
2008	1,041	474	66
2009	1,031	373	67
2010	1,005	40	69
2011	951	6	18
2012	908		
2013 and thereafter	5,562		
<b>Total</b>	<b>Ps. 11,535</b>	<b>Ps. 1,593</b>	<b>Ps. 291</b>

Rental expense charged to operations amounted to approximately Ps. 1,468, Ps. 1,619 and Ps. 1,217 for the years ended December 31, 2006, 2005 and 2004, respectively.

**Table of Contents****Note 26. Information by Segment.****a) By Business Unit:**

	Coca-Cola	FEMSA	FEMSA		Consolidation	
<b>2006</b>	FEMSA	Cerveza	Comercio	Other	Adjustments	Consolidated
Total revenue	Ps. 57,738	Ps. 35,599	Ps. 35,500	Ps. 7,678	Ps. (10,088)	Ps. 126,427
Intercompany revenue	696	3,598	12	5,782	(10,088)	
Income from operations	9,456	5,915	1,604	415		17,390
Depreciation <sup>(1)</sup>	2,393	1,684	415	107		4,599
Amortization	208	1,928	350	34		2,520
Other non-cash charges <sup>(2) (3)</sup>	178	223	15	85		501
Impairment of long-lived assets	76	117		7		200
Interest expense	2,124	1,531	388	506	(509)	4,040
Interest income	315	219	51	631	(509)	707
Income tax	2,318	1,423	347	208		4,296
Capital expenditures	2,615	4,212	1,873	188		8,888
Long-term assets	63,952	45,765	7,626	7,614	(4,976)	119,981
Total assets	75,024	58,588	11,865	10,390	(10,477)	145,390
<b>2005</b>						
Total revenue	Ps. 53,997	Ps. 28,690	Ps. 29,898	Ps. 6,250	Ps. (7,199)	Ps. 111,636
Intercompany revenue	627	2,151	2	4,419	(7,199)	
Income from operations	9,218	5,590	1,310	285		16,403
Depreciation <sup>(1)</sup>	2,385	1,558	336	103		4,382
Amortization	168	1,813	290	15		2,286
Other non-cash charges <sup>(2) (3)</sup>	160	156	7	66		389
Impairment of long-lived assets		79		2		81
Interest expense	2,591	1,264	367	733	(435)	4,520
Interest income	311	218	67	523	(435)	684
Income tax	2,455	1,143	298	404		4,300
Capital expenditures	2,219	3,086	1,472	257		7,034
Long-term assets	62,698	37,454	6,533	7,963	(5,438)	109,210
Total assets	71,034	46,625	10,082	11,823	(7,252)	132,312
<b>2004</b>						
Total revenue	Ps. 51,276	Ps. 26,848	Ps. 24,556	Ps. 5,610	Ps. (5,974)	Ps. 102,316
Intercompany revenue	295	1,735	2	3,942	(5,974)	
Income from operations	8,459	5,101	979	425		14,964
Depreciation <sup>(1)</sup>	2,177	1,604	232	112		4,125
Amortization	309	1,803	236	33		2,381
Other non-cash charges <sup>(2) (3)</sup>	65	209	16	53		343
Impairment of long-lived assets		495		14		509
Interest expense	2,753	864	234	527	(302)	4,076
Interest income	317	169	55	374	(302)	613
Income tax	920	860	256	167		2,203
Capital expenditures	2,162	3,409	1,772	165		7,508

(1) Includes breakage of bottles.



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- (2) Excludes the non-cash charges related to current assets and liabilities.
  
- (3) Includes the cost for the year related to labor liabilities (see Note 17 d) and participation in associated companies.

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**Table of Contents****b) By Geographic Area:**

	Total	Capital	Long-term	Total
2006	Revenue	Expenditures	Assets	Assets
Mexico	Ps. 95,795	Ps. 7,524	Ps. 92,100	Ps. 110,888
Central America <sup>(1)</sup>	4,145	73	5,297	6,214
Colombia	5,586	499	6,458	9,207
Venezuela	6,536	181	3,750	4,935
Brazil	11,340	402	10,997	15,711
Argentina	3,281	209	1,379	2,219
Consolidation adjustments	(256)			(3,784)
Consolidated	Ps. 126,427	Ps. 8,888	Ps. 119,981	Ps. 145,390

	Total	Capital	Long-term	Total
2005	Revenue	Expenditures	Assets	Assets
Mexico	Ps. 87,281	Ps. 5,715	Ps. 87,778	Ps. 107,084
Central America <sup>(1)</sup>	3,636	197	4,810	5,823
Colombia	5,238	368	6,427	9,106
Venezuela	5,875	412	3,953	4,935
Brazil	6,650	204	4,879	7,196
Argentina	3,090	138	1,363	1,955
Consolidation adjustments	(134)			(3,787)
Consolidated	Ps. 111,636	Ps. 7,034	Ps. 109,210	Ps. 132,312

	Total	Capital
2004	Revenue	Expenditures
Mexico	Ps. 79,634	Ps. 6,532
Central America <sup>(1)</sup>	3,736	173
Colombia	4,734	137
Venezuela	5,563	279
Brazil	5,865	324
Argentina	2,871	63
Consolidation adjustments	(87)	
Consolidated	Ps. 102,316	Ps. 7,508

(1) Includes Guatemala, Nicaragua, Costa Rica and Panama.

**Note 27. Differences Between Mexican FRS and U.S. GAAP.**

As discussed in Note 2, the consolidated financial statements of the Company are prepared in accordance with Mexican FRS, which differs in certain significant respects from U.S. GAAP. A reconciliation of the reported majority net income, majority stockholders' equity and majority comprehensive income to U.S. GAAP is presented in Note 28. It should be noted that this reconciliation to U.S. GAAP does not include the reversal of the restatement of the financial statements as required by Bulletin B-10, Reconocimiento de los Efectos de la Inflación en la Información Financiera (Recognition of the Effects of Inflation in the Financial Information), of Mexican FRS.

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The application of this Bulletin represents a comprehensive measure of the effects of price-level changes in the Mexican economy and, as such, is considered a more meaningful presentation than historical cost-based financial reporting in Mexican pesos for both Mexican and U.S. accounting purposes.

The principal differences between Mexican FRS and U.S. GAAP included in the reconciliation that affect the consolidated financial statements of the Company are described below.

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**a) Consolidation of Coca-Cola FEMSA:**

Under Mexican FRS, the Company consolidates Coca-Cola FEMSA since it owns a majority of the outstanding voting capital stock and exercises control over the operations of Coca-Cola FEMSA in the ordinary course of business in accordance with the requirements of Mexican Bulletin B-8, Estados Financieros Consolidados y Combinados y Valuación de Inversiones Permanentes en Acciones (Consolidated and Combined Financial Statements and Valuation of Long-Term Investments in Shares). Pursuant to Bulletin B-8, Coca-Cola FEMSA meets the criteria of a subsidiary for consolidation as FEMSA holds more than 50% of Coca-Cola FEMSA's outstanding voting stock and has not yielded control to a minority shareholder. Bulletin B-8 establishes that control has been yielded when a minority shareholder obtains:

Control over more than 50% of the voting rights through a formal agreement with other shareholders;

The power derived from by-laws or formal agreement by shareholders to govern the operating and financial policies of a company;

The power to appoint or remove a majority of the Board of Directors or any organization that governs the operating and financial policies of the Company; or

The power to decide the majority of the votes of the Board of Directors.

No minority shareholder of Coca-Cola FEMSA has obtained any of the rights described above.

The shareholders agreement grants The Coca-Cola Company substantive participating rights. The affirmative vote of two Directors appointed by The Coca-Cola Company is, with limited exceptions, required for matters considered by the Board of Directors, including the annual business plan, capital investment plan and asset disposals, mergers, acquisitions or sales of any line of business. Under Emerging Issues Task Force (EITF) 96-16, Investor's Accounting for an Investee When the Investor Owns a Majority of the Voting Stock but the Minority Shareholder or Shareholders Have Certain Approval or Veto Rights such approval and veto rights held by The Coca-Cola Company qualify as substantive participating rights and therefore do not allow FEMSA to consolidate Coca-Cola FEMSA in its financial statements for U.S. GAAP purposes. Therefore, FEMSA's investment in Coca-Cola FEMSA is recorded by applying the equity method in FEMSA's consolidated financial statements under U.S. GAAP.

As mentioned in Note 5, in 2006 FEMSA indirectly acquired an additional, 8.02% of the total outstanding equity of Coca-Cola FEMSA. According to Mexican FRS Bulletin B-7, this is a transaction between shareholders that does not impact the net assets of the Company, and the payment in excess of the book value of the shares acquired is recorded in stockholders' equity as a reduction of additional paid-in capital. Under US GAAP, Statement of Financial Accounting Standards (SFAS) No. 141, Business Combinations, purchases of minority interest represent a step acquisition that must be recorded by the purchase method, whereby the purchase price is allocated to the proportionate fair value of assets and liabilities acquired. As of December 31, 2006, the purchase price allocation for this acquisition has not been completed, and the allocation period is open. The difference between the fair value and the price paid for the 8.02% of Coca-Cola FEMSA equity is presented as part of investment in Coca-Cola FEMSA shares in the consolidated balance sheet under U.S. GAAP. The Company does not anticipate recognizing any goodwill as a result of this acquisition.

Summarized consolidated balance sheets and income statements of Coca-Cola FEMSA and subsidiaries under U.S. GAAP as of December 31, 2006 and 2005 and for the years ended December 31, 2006, 2005 and 2004 are presented as follows:

<b>Consolidated Balance Sheets</b>	<b>2006</b>	<b>2005</b>
Current assets	<b>Ps. 11,509</b>	Ps. 7,979
Property, plant and equipment	<b>20,472</b>	19,867
Other assets	<b>43,727</b>	42,694
 Total assets	 <b>Ps. 75,708</b>	 Ps. 70,540
 Current liabilities	 <b>Ps. 12,161</b>	 Ps. 12,590

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Long-term liabilities	<b>22,076</b>	21,821
<b>Total liabilities</b>	<b>34,237</b>	34,411
Minority interest in consolidated subsidiaries	<b>1,214</b>	998
<b>Stockholders' equity</b>	<b>40,257</b>	35,131
 Total liabilities and stockholders' equity	 <b>Ps. 75,708</b>	 Ps. 70,540

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<b>Consolidated Income Statements</b>	<b>2006</b>	2005	2004
Total revenues	<b>Ps. 57,568</b>	Ps. 52,233	Ps. 49,351
Income from operations	<b>8,432</b>	8,423	7,837
Income before income tax	<b>7,421</b>	7,154	6,809
Income tax	<b>2,332</b>	2,382	619
Minority interest in results of consolidated subsidiaries	<b>170</b>	123	25
Net income	<b>4,919</b>	4,649	6,165
Other comprehensive income	<b>986</b>	(324)	943
Comprehensive income	<b>Ps. 5,905</b>	Ps. 4,325	Ps. 7,108

**b) Restatement for Inflation of Prior Year Financial Statements:**

As explained in Note 4 a), in accordance with Mexican FRS, the financial statements for Mexican subsidiaries for prior years were restated using inflation factors and for foreign subsidiaries and affiliated companies for prior years were restated using the inflation rate of the country in which the foreign subsidiary or affiliated company is located, then translated to Mexican pesos at the year-end exchange rate.

Under U.S. GAAP, the Company applies the regulations of the Securities and Exchange Commission of the United States of America ( SEC ), which require that prior year financial statements be restated in constant units of the reporting currency, in this case the Mexican peso, which requires the restatement of such prior year amounts using Mexican inflation factors.

Additionally, all other U.S. GAAP adjustments for prior years have been restated based upon such methodology.

**c) Classification Differences:**

Certain items require a different classification in the balance sheet or income statement under U.S. GAAP. These include:

As explained in Note 4 c), under Mexican FRS, advances to suppliers are recorded as inventories. Under U.S. GAAP advances to suppliers are classified as prepaid expenses;

Impairment of goodwill and other long-lived assets, the gains or losses on the disposition of fixed assets, all severance indemnity charges and employee profit sharing must be included in operating expenses under U.S. GAAP; and

Under Mexican FRS, deferred taxes are classified as non-current, while under U.S. GAAP they are based on the classification of the related asset or liability.

**d) Deferred Promotional Expenses:**

As explained in Note 4 d), for Mexican FRS purposes, the promotional costs related to the launching of new products or presentations are recorded as prepaid expenses. For U.S. GAAP purposes, such promotional costs are expensed as incurred. As of December 31, 2006 and 2005, this difference was reconciled by Coca-Cola FEMSA and its impact in FEMSA is included in the participation of Coca-Cola FEMSA. No other consolidated entity has deferred promotional expenses.

**e) Start-up Expenses:**

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As explained in Note 4 i), under Mexican FRS, start-up expenses are capitalized and amortized using the straight-line method in accordance with the terms of the lease contracts at the start of operations. Under U.S. GAAP, these expenses must be recorded in the income statement as incurred, except for the licenses for the sale of beer paid for by FEMSA Comercio, which are considered to be intangible assets and amortized using the straight-line method beginning at the start of operations.

**f) Intangible Assets:**

As mentioned in Note 4 i), under Mexican FRS, until January 1, 2003, all intangible assets were amortized over a period of no more than 20 years. Effective January 1, 2003, revised Bulletin C-8, Activos Intangibles (Intangible Assets), went into effect and recognizes that certain intangible assets (excluding goodwill) have indefinite lives and should not be amortized. In accordance with SFAS No. 142, Goodwill and Other Intangible Assets (effective January 1, 2002), goodwill and indefinite-lived intangible assets are also no longer subject to amortization, but rather are subject to periodic assessment for impairment. Accordingly, amortization of indefinite-lived intangible assets was discontinued in 2002 for U.S. GAAP. In 2003 amortization of indefinite-lived intangible assets was discontinued for Mexican FRS and in 2004 the amortization of goodwill was discontinued (see Note 4 i).

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As a result of adopting SFAS No. 142, the Company performed an initial impairment test as of January 1, 2002 and found no impairment. Subsequent impairment tests are performed annually by the Company, unless an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. In such case an impairment test would be performed between annual tests.

### **g) Restatement of Imported Equipment for Inflation:**

As explained in Note 4 g), under Mexican FRS, imported machinery and equipment have been restated by applying the inflation rate of the country of origin and translated into Mexican pesos using the year-end rate.

Under U.S. GAAP, the Company applies the regulations of the SEC, which require that all machinery and equipment, both domestic and imported, be restated using Mexican inflation factors.

### **h) Capitalization of the Integral Result of Financing:**

Under Mexican FRS, the capitalization of the integral result of financing (interest, foreign exchange and monetary position) generated by loan agreements obtained to finance investment projects is optional, and the Company has elected not to capitalize the integral result of financing.

In accordance with SFAS No. 34, Capitalization of Interest Cost, if the integral result of financing is incurred during the construction of qualifying assets, capitalization is required for all assets that require a period of time to get them ready for their intended use. Accordingly, a reconciling item for the capitalization of a portion of the integral result of financing is included in the U.S. GAAP reconciliation of the majority net income and majority stockholders' equity. If the borrowings are denominated in U.S. dollars, the weighted average interest rate on all such outstanding debt is applied to the balance of construction-in-progress to determine the amount to be capitalized. If the borrowings are denominated in Mexican pesos, the amount of interest to be capitalized as noted above is reduced by the gain on monetary position associated with the debt.

### **i) Derivative Financial Instruments:**

As of January 1, 2005, in accordance with Mexican FRS, as mentioned in Note 4 q), the Company values and records all derivative financial instruments and hedging activities according to Bulletin C-10, Instrumentos Financieros Derivados y Operaciones de Cobertura (Derivative Financial Instruments and Hedging Activities), which establishes similar accounting treatment as described in SFAS No. 133, Accounting for Derivative Financial Instruments and Hedging Activities. Therefore, as of such date the Company no longer has any difference as it relates to derivative financial instruments.

### **j) Deferred Income Tax and Employee Profit Sharing:**

The Company calculates its deferred income tax and employee profit sharing in accordance with SFAS No. 109, Accounting for Income Taxes, for U.S. GAAP purposes, which differs from Mexican FRS as follows:

Under Mexican FRS, the effects of inflation on the deferred tax balance generated by monetary items are recognized in the result of monetary position. Under U.S. GAAP, the deferred tax balance is classified as a non-monetary item. As a result, the consolidated income statement differs with respect to the presentation of the gain or loss on monetary position and deferred income tax provision;

Under Mexican FRS, deferred employee profit sharing is calculated considering only those temporary differences that arise during the year and which are expected to reverse within a defined period, while under U.S. GAAP, the same liability method used for deferred income tax is applied; and



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The differences in start-up expenses, restatement of imported machinery and equipment, capitalization of financing costs, financial instruments and pension plan mentioned in Note 27 d), f), g), h) and j) generate a difference when calculating the deferred income tax under U.S. GAAP compared to that presented under Mexican FRS (see Note 24 d).

As explained in Note 24 a), the 2005 employee profit sharing to be paid in 2006 will be deductible for income tax purposes in Mexico. This new deduction will reduce the payments of income tax in subsequent years. Therefore, the Company recorded a reduction to the deferred income tax liability under U.S. GAAP of Ps. 175 and Ps. 250 as of December 31, 2006 and 2005, respectively.

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The reconciliation of deferred income tax and employee profit sharing, as well as the changes in the balances of deferred taxes, are as follows:

<b>Reconciliation of Deferred Income Tax, net</b>	<b>2006</b>	<b>2005</b>
Deferred income tax under Mexican FRS	<b>Ps. 2,107</b>	Ps. 2,142
Deferred income tax of Coca-Cola FEMSA	<b>133</b>	318
U.S. GAAP adjustments:		
Start-up expenses	<b>(53)</b>	(51)
Restatement of imported equipment	<b>84</b>	164
Capitalization of integral result of financing	<b>98</b>	112
Tax deduction for employee profit sharing	<b>(175)</b>	(250)
Labor liabilities	<b>(451)</b>	(95)
<b>Total U.S. GAAP adjustments</b>	<b>(497)</b>	(120)
 Deferred income tax, net under U.S. GAAP	 <b>Ps. 1,743</b>	 Ps. 2,340

The total deferred income tax under U.S. GAAP includes the corresponding current portion as of December 31, 2006 and 2005 of Ps. 286 and Ps. 959, respectively.

<b>Changes in the Balance of Deferred Income Tax</b>	<b>2006</b>	<b>2005</b>
Initial balance	<b>Ps. 2,340</b>	Ps. 2,720
SFAS No. 158 adjustment	<b>(310)</b>	
Provision for the year	<b>(230)</b>	(240)
Derivative financial instruments	<b>(67)</b>	(110)
Additional labor liability over unrecognized net transition obligation		(19)
Change in the statutory income tax rate	<b>10</b>	(11)
<b>Ending balance</b>	<b>Ps. 1,743</b>	Ps. 2,340

<b>Reconciliation of Deferred Employee Profit Sharing</b>	<b>2006</b>	<b>2005</b>
Deferred employee profit sharing under Mexican FRS	<b>Ps.</b>	Ps.
U.S. GAAP adjustments:		
Allowance for doubtful accounts	<b>(6)</b>	(6)
Inventories	<b>124</b>	212
Prepaid expenses	<b>27</b>	33
Property, plant and equipment	<b>939</b>	929
Deferred charges	<b>(129)</b>	(94)
Intangible assets	<b>1</b>	7
Capitalization of interest expense	<b>35</b>	40
Start-up expenses	<b>(16)</b>	(15)
Derivative financial instruments	<b>3</b>	5
Labor liabilities	<b>(286)</b>	(162)
Other reserves	<b>(66)</b>	(55)
<b>Total U.S. GAAP adjustments</b>	<b>626</b>	894
 Deferred employee profit sharing under U.S. GAAP	 <b>Ps. 626</b>	 Ps. 894

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The total deferred employee profit sharing under U.S. GAAP includes the corresponding current portion as of December 31, 2006 and 2005 of Ps. 148 and Ps. 244, respectively.

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<b>Changes in the Balance of Deferred Employee Profit Sharing</b>	<b>2006</b>	<b>2005</b>
Initial balance	<b>Ps. 894</b>	Ps. 1,140
SFAS No. 158 adjustment	<b>(125)</b>	
Provision for the year	<b>(143)</b>	(240)
Additional labor liability over unrecognized net transition obligation		(6)
<b>Ending balance</b>	<b>Ps. 626</b>	Ps. 894

**k) Labor Liabilities:**

Under Mexican FRS, the liabilities for employee benefits are determined using actuarial computations in accordance with Bulletin D-3 which is substantially the same as SFAS No. 87, Employers Accounting for Pensions, except for the initial year of application of both standards, which generates a difference in the unamortized net transition obligation and in the amortization expense.

In January 1997, as a result of the application of inflationary accounting, Mexican FRS determined that labor obligations are non-monetary liabilities and required the application of real, instead of nominal, interest rates in actuarial calculations. These changes required recalculation of the accumulated transition obligation, and the difference in the transition obligation represents the sum of the actuarial gains or losses since the first year that labor obligations have been calculated.

The Company uses the same real interest rate for both U.S. GAAP and Mexican FRS. As a result, the transition obligation has been recalculated and the difference is being amortized over the average life of employment of the Company.

Under Mexican FRS, as mentioned in Note 4 l), effective in 2005 revised Bulletin D-3 requires the recognition of a severance indemnity liability calculated based on actuarial computations. The same recognition criteria under U.S. GAAP is established in SFAS No. 112 Employers Accounting for Postemployment Benefits, which has been effective since 1994. The Company had not previously recorded an amount under U.S. GAAP as it believed that an obligation could not be reasonably quantified.

Beginning in 2005, the Company applies the same considerations as required by Mexican FRS to recognize the severance indemnity liability for U.S. GAAP purposes. The cumulative effect of the severance obligation related to vested services was recorded in the 2005 income statement since the effect was not considered to be quantitatively or qualitatively material to the Company's consolidated U.S. GAAP financial statements taken as a whole. The additional labor liability has not been recorded for U.S. GAAP purposes.

The Company adopted 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), in its December 31, 2006 consolidated financial statements. This statement requires companies to (1) fully recognize, as an asset or liability, the overfunded or underfunded status of defined pension and other postretirement benefit plans; (2) recognize changes in the funded status through other comprehensive income in the year in which the changes occur; and (3) provide enhanced disclosures. The impact of adoption, including the interrelated impact on the minimum pension liability, resulted in an increase in total liabilities and a decrease in stockholders' equity reported under U.S. GAAP of Ps. 185 and Ps. 860, respectively.

Prior to the adoption of SFAS No. 158, there was no difference in the liabilities for seniority premiums and postretirement medical benefits between Mexican FRS and U.S. GAAP.

The reconciliation of the cost for the year and labor liabilities is as follows:

<b>Cost for the Year</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
Net cost recorded under Mexican FRS	<b>Ps. 521</b>	Ps. 468	Ps. 321
Net cost of Coca-Cola FEMSA	<b>(140)</b>	(167)	(71)
U.S. GAAP adjustments:			
Amortization of unrecognized transition obligation	<b>(5)</b>	269	30
<b>Cost for the year under U.S. GAAP</b>	<b>Ps. 376</b>	Ps. 570	Ps. 280



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	December 2006 SFAS			December 2005
	Before SFAS No. 158	No. 158	After SFAS No. 158	
<b>Labor Liabilities</b>	<b>Ps. 3,115</b>	<b>Ps.</b>	<b>Ps. 3,115</b>	<b>Ps. 2,556</b>
Labor liabilities under Mexican FRS				
Labor liabilities of Coca-Cola FEMSA	(862)		(862)	(820)
U.S. GAAP adjustments:				
Unrecognized net transition obligation	265	1,038	1,303	284
Unrecognized net actuarial loss	61	379	440	42
Additional labor liability in accumulated other comprehensive income		(122)	(122)	
U.S.GAAP adjustments to stockholders equity	326	1,295	1,621	326
Additional severance indemnity liability	(244)		(244)	
Additional pension plan liability	(51)	(675)	(726)	
Total U.S. GAAP adjustment	31	620	651	326
Labor liabilities under U.S. GAAP	Ps. 2,284	Ps. 620	Ps. 2,904	Ps. 2,062

The incremental effect of this adoption on the individual line items in the December 31, 2006 consolidated U.S. GAAP balance sheet is shown in the following table:

	SFAS		
	Before	No. 158	After
<b>Application of SFAS No. 158</b>			
Assets:			
Other assets	Ps. 8,419	Ps. (675)	Ps. 7,744
Total assets	111,213	(675)	110,538
Long-term liabilities:			
Deferred income tax liability	2,053	(310)	1,743
Deferred employee profit sharing	751	(125)	626
Labor liabilities	2,284	620	2,904
Total liabilities	38,947	185	39,133
Accumulated other comprehensive income:			
Labor liabilities	(108)	(860)	(968)
Total stockholders equity	72,106	(860)	71,246
Total liabilities and stockholders equity	Ps. 111,213	Ps. (675)	Ps. 110,538

Estimates of the unrecognized items expected to be recognized as components of net periodic pension cost during 2007 are shown in the table below:

Pension and	Seniority Premiums	Postretirement Medical
----------------	-----------------------	---------------------------

	Retirements		Services			
	Plans					
Net transition obligation	Ps.	48	Ps.	1	Ps.	5
Prior service cost		48				
Net actuarial loss		2		1		7
	Ps.	98	Ps.	2	Ps.	12

**l) Kaiser Minority Acquisition:**

As mentioned in Note 6a), in 2006 FEMSA Cerveza indirectly acquired an additional equity interest in Kaiser. According to Mexican FRS Bulletin B-7, this is a transaction between shareholders that does not impact the net assets of the Company, and the payment in excess of the book value of the shares acquired is recorded in stockholders' equity as a reduction of additional paid-in-capital. Under US GAAP, SFAS No. 141, purchases of minority interest represent a step acquisition that must be recorded by the purchase method, whereby the purchase price is allocated to the proportionate fair value of assets and liabilities acquired. As of December 31, 2006 the purchase price allocation for this acquisition has not been completed, and the allocation period is open. The Company does not anticipate recognizing any goodwill as a result of this acquisition.

**m) Minority Interest:**

Under Mexican FRS, the minority interest in consolidated subsidiaries is presented as a separate component within stockholders' equity in the consolidated balance sheet.

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Under U.S. GAAP, this item must be excluded from consolidated stockholders' equity in the consolidated balance sheet. Additionally, the minority interest in the net earnings of consolidated subsidiaries is excluded from consolidated net income.

The U.S. GAAP adjustments shown in Note 28 a) and b) are calculated on a consolidated basis. Therefore, the minority interest effects are presented as a separate line item to obtain net income and stockholders' equity.

The U.S. GAAP adjustments corresponding to FEMSA Cerveza's minority interest, includes amounts until the date of acquisition of the FEMSA Cerveza minority interest in 2004 which represented a loss of Ps. 8 in 2004 (see Note 6).

**n) FEMSA's Minority Interest Acquisition:**

In accordance with Mexican FRS, the Company applied the entity theory to the acquisition of the minority interest by FEMSA in May 1998, through an exchange offer. Accordingly, no goodwill was created as a result of such acquisition and the difference between the book value of the shares acquired by FEMSA and the FEMSA shares exchanged was recorded as additional paid-in capital. The direct out-of-pocket costs identified with the purchase of minority interest are treated as an additional purchase cost and included in other expenses.

In accordance with U.S. GAAP, the acquisition of minority interest must be accounted under the purchase method, using the market value of shares received by FEMSA in the exchange offer to determine the cost of the acquisition of such minority interest and the related goodwill. Under U.S. GAAP, the direct out-of-pocket costs identified with the purchase of minority interest are treated as additional goodwill.

Additionally, SFAS No. 142 requires the allocation of all goodwill to the related reporting units. The allocation of the goodwill generated by the previously mentioned acquisition of minority interest is as follows:

FEMSA Cerveza	Ps. 10,216
Coca-Cola FEMSA	4,581
FEMSA Comercio	1,046
Other companies	883
	Ps. 16,726

**o) Earnings per Share:**

At its annual general ordinary shareholders' meeting held on March 29, 2007, the Company's shareholders approved a three-for-one stock split in respect to all of its outstanding capital stock. Following the stock split, FEMSA's total capital stock consists of 2,161,177,770 BD Units and 1,417,048,500 B Units. The stock split also resulted in a three-for-one stock split of the Company's ADSs. The stock-split was conducted on a pro-rata basis in respect of all holders of record of the Company's shares and ADSs as of May 25, 2007, and the ratio of voting and non-voting shares was maintained, thereby preserving the ownership structure as it was prior to the stock split.

Mexican FRS, Bulletin B-14 Utilidad por acción (Earnings per share) and SFAS No. 128, Earnings per Share, require that changes in common stock resulting from stock splits occurring after the close of the period but before issuance of the financial statements must reflect the per-share computations for those and any prior-period financial statements presented based on the new number of shares. Additionally, Mexican FRS, Bulletin A-7 Presentación y Revelación (Presentation and Disclosure) states that an entity should disclose the date financial statements were authorized for issuance and by whom and as a result they do not reflect events occurring after such date. FEMSA's consolidated financial statements were approved and issued by its Board of Directors on February 23, 2007 (see Note 2).

As a result, under Mexican FRS, the consolidated financial statements do not include the effects of such stock split.

For US GAAP purposes, SFAS No.128 Earnings per Share is similar to Mexican Bulletin B-14; however EITF D-86, Issuance of Financial Statements, specifies that financial statements must consider all subsequent events up through the issuance date of the financial statements. This EITF clarifies that financial statements are issued as of the date they are distributed for general use and reliance in a form and format that complies with generally accepted accounting principles (GAAP) and, in the case of annual financial statements, that contain an audit report that



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indicates that the auditors have complied with generally accepted auditing standards (GAAS) in completing their audit. The significance of the date on which the financial statements are considered issued is that this is the date up to which subsequent events should be considered in terms of the potential effect on the financial statements and may result in adjustments to the financial statements. For U.S. GAAP purposes the financial statements were not considered issued as of May 25, 2007, given that the Company's independent registered public accounting firm had not finalized procedures as required by the Public Company Accounting Oversight Board (United States).

As the Company's U.S. GAAP financial information is not considered to be issued as of May 25, 2007, earnings-per-share has been retroactively restated to give effects to the stock split in accordance with SFAS No. 128.

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The following table present the original number of shares and the effects of the three for one stock split for the years ended December 31, 2006, 2005 and 2004:

	Millions of Shares		
	2006	2005	2004
<b>Series B</b>			
Original			
Number of shares	<b>3,082.14</b>	3,082.14	2,737.74
Weighted average	<b>3,082.14</b>	2,944.95	2,739.17
Split effect (3:1)			
Number of shares	<b>9,246.42</b>	9,246.42	8,213.22
Weighted average	<b>9,246.42</b>	8,834.85	8,217.51
<b>Series D</b>			
Original			
Number of shares	<b>2,881.57</b>	2,881.57	2,559.57
Weighted average	<b>2,881.57</b>	2,753.38	2,561.00
Split effect (3:1)			
Number of shares	<b>8,644.71</b>	8,644.71	7,678.71
Weighted average	<b>8,644.71</b>	8,260.14	7,683.00

**p) Statement of Cash Flows:**

Under Mexican FRS, the Company presents a consolidated statement of changes in financial position in accordance with Bulletin B-12, Estado de Cambios en la Situación Financiera (Statement of Changes in Financial Position), which identifies the generation and application of resources by the differences between beginning and ending financial statement balances in constant Mexican pesos. Bulletin B-12 also requires that monetary and foreign exchange gains and losses be treated as cash items for the determination of resources generated by operations.

In accordance with U.S. GAAP, the Company follows SFAS No. 95, Statement of Cash Flows, which is presented in historical Mexican pesos, without the effects of inflation (see Note 27 p).

**Table of Contents****q) Financial Information Under U.S. GAAP:**

Consolidated Balance Sheets	2006	2005
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and cash equivalents	Ps. 3,463	Ps. 6,432
Accounts receivable	4,830	2,867
Inventories	5,275	4,310
Recoverable taxes	668	358
Other current assets	652	591
 Total current assets	 14,888	 14,558
<b>Investments in shares:</b>		
Coca-Cola FEMSA	23,172	16,058
Other investments	358	331
Property, plant and equipment	30,022	27,036
Intangible assets	32,697	27,909
Bottles and cases	1,647	1,416
Other assets	7,754	7,978
 <b>TOTAL ASSETS</b>	 <b>Ps. 110,538</b>	 <b>Ps. 95,286</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
<b>Current Liabilities:</b>		
Bank loans	Ps. 2,399	Ps. 47
Interest payable	156	79
Current maturities of long-term debt	361	427
Suppliers	6,847	4,907
Deferred tax liability	434	1,362
Taxes payable	1,519	980
Accounts payable, accrued expenses and other liabilities	2,562	1,922
 Total current liabilities	 14,278	 9,724
<b>Long-Term Liabilities:</b>		
Bank loans and notes payable	18,070	14,627
Deferred tax liability	1,945	1,881
Labor liabilities	2,904	2,062
Other liabilities	1,935	872
 Total long-term liabilities	 24,854	 19,442
 <b>Total liabilities</b>	 <b>39,132</b>	 <b>29,166</b>
<b>Minority interest in consolidated subsidiaries</b>	<b>160</b>	<b>50</b>
<b>Stockholders equity</b>	<b>71,246</b>	<b>66,070</b>
 <b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>	 <b>Ps. 110,538</b>	 <b>Ps. 95,286</b>

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<b>Consolidated Income Statements</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
Net sales	<b>Ps. 72,558</b>	Ps. 60,439	Ps. 53,101
Other operating revenues	<b>401</b>	310	443
<b>Total revenues</b>	<b>72,959</b>	60,749	53,544
Cost of sales	<b>42,462</b>	35,268	29,373
<b>Gross profit</b>	<b>30,497</b>	25,481	24,171
Operating expenses:			
Administrative	<b>5,483</b>	4,904	4,405
Selling	<b>17,478</b>	13,915	13,973
	<b>22,961</b>	18,819	18,378
Income from operations	<b>7,536</b>	6,662	5,793
Integral result of financing:			
Interest expense	<b>(1,930)</b>	(1,783)	(1,273)
Interest income	<b>406</b>	372	296
Foreign exchange gain	<b>11</b>	(14)	25
Gain on monetary position	<b>413</b>	275	481
Market value gain (loss) on ineffective portion of derivative financial instruments	<b>5</b>	(89)	
	<b>(1,095)</b>	(1,239)	(471)
Other expenses, net	<b>(287)</b>	(91)	93
Income before income tax and tax on assets	<b>6,154</b>	5,332	5,415
Income tax and tax on assets	<b>1,955</b>	1,661	722
Income before minority interest and affiliated companies	<b>4,199</b>	3,671	4,693
Minority interest in results of consolidated subsidiaries	<b>163</b>		(505)
Participation in affiliated companies:			
Coca-Cola FEMSA	<b>2,332</b>	2,125	2,830
Other affiliated companies	<b>26</b>	44	68
	<b>2,358</b>	2,169	2,898
Net income	<b>Ps. 6,720</b>	Ps. 5,840	Ps. 7,086
Other comprehensive income (loss)	<b>333</b>	(1,033)	(224)
Comprehensive income	<b>Ps. 7,053</b>	Ps. 4,807	Ps. 6,862
Net income per share (constant Mexican pesos) <sup>(1)</sup> :			
Per Series B share	<b>Ps. 0.34</b>	Ps. 0.30	Ps. 0.40
Per Series D share	<b>0.42</b>	0.38	0.50

(1) Reflects 3:1 stock split effective May 25, 2005 (see Note 27 O).

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Consolidated Cash Flows <sup>(1)</sup>	2006	2005	2004
<b>Cash flows from operating activities:</b>			
Net income	Ps. 6,720	Ps. 5,840	Ps. 7,086
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Minority interest	(163)		505
Inflation effect	(463)	(325)	(671)
Depreciation	2,080	1,930	1,776
Amortization	2,416	1,998	1,919
Participation in affiliated companies	(2,332)	(2,077)	(2,695)
Deferred income taxes	(383)	(367)	(605)
Other non-cash charges	1,332	586	274
Changes in operating assets and liabilities net of business acquisitions:			
Working capital investment	(3,026)	357	(661)
Dividends received from Coca-Cola FEMSA	317	283	238
Recoverable taxes, net	(481)	(547)	(691)
Interest payable	80	(5)	56
Labor obligations	(366)	(168)	306
<b>Net cash flows provided by operating activities</b>	<b>5,731</b>	<b>7,505</b>	<b>6,837</b>
<b>Cash flows from investing activities:</b>			
Acquisition of Coca-Cola FEMSA minority interest	(4,601)		
Acquisitions by FEMSA Cerveza, net of cash acquired	(1,711)		
Property, plant and equipment	(3,091)	(2,169)	(1,798)
Other assets	(3,091)	(3,002)	(2,304)
Bottles and cases	(95)	(57)	(111)
Investment in shares	7		
Acquisition of FEMSA Cerveza minority interest			(14,694)
<b>Net cash flows used in investing activities</b>	<b>(12,582)</b>	<b>(5,228)</b>	<b>(18,907)</b>
<b>Cash flows from financing activities:</b>			
Bank loans obtained	6,229	16	17,043
Bank loans paid	(604)	(5,982)	(5,529)
Issuance of capital stock		7,644	
Dividends declared and paid	(986)	(660)	(531)
Derivative financial instruments	(498)	(221)	(377)
Other financing activities	6	(80)	(162)
<b>Net cash flows provided by (used in) financing activities</b>	<b>4,147</b>	<b>717</b>	<b>10,444</b>
Effect of exchange rate changes on cash and cash equivalents	(15)	(32)	(104)
<b>Cash and cash equivalents:</b>			
Net increase (decrease)	(2,719)	2,962	(1,730)
Initial balance	6,182	3,220	4,950
<b>Ending balance</b>	<b>Ps. 3,463</b>	<b>Ps. 6,182</b>	<b>Ps. 3,220</b>
<b>Supplemental cash flow information:</b>			
Interest paid	Ps. 1,804	Ps. 2,033	Ps. 1,153
Income tax and tax on assets paid	2,463	2,150	2,130

(1) Expressed in millions of historical Mexican pesos.

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<b>Consolidated Statements of Changes in Stockholders' Equity</b>	<b>2006</b>	<b>2005</b>
Stockholders' equity at the beginning of the year	<b>Ps. 66,070</b>	Ps. 53,814
Increase in capital stock		8,153
Dividends declared and paid	<b>(1,017)</b>	(704)
SFAS No. 158 adjustment	<b>(860)</b>	
Other comprehensive income (loss):		
Derivative financial instruments	<b>(151)</b>	(136)
Additional labor liability over unrecognized net transition obligation	<b>24</b>	(40)
Cumulative translation adjustment	<b>(103)</b>	(110)
Result of holding non-monetary assets	<b>563</b>	(747)
Other comprehensive income (loss)	<b>333</b>	(1,033)
Net income	<b>6,720</b>	5,840
Stockholders' equity at the end of the year	<b>Ps. 71,246</b>	Ps. 66,070

**Note 28. Reconciliation of Mexican FRS to U.S. GAAP.****a) Reconciliation of Net Income:**

	<b>2006</b>	<b>2005</b>	<b>2004</b>
Net majority income under Mexican FRS	<b>Ps. 6,622</b>	Ps. 5,766	Ps. 6,411
U.S. GAAP adjustments:			
Restatement of prior year financial statements		8	(140)
Participation in Coca-Cola FEMSA (Note 27 a)	<b>13</b>	(55)	175
Start-up expenses (Note 27 e)	<b>(14)</b>	(21)	(25)
Intangible assets and goodwill (Note 27 f)			15
Restatement of imported machinery and equipment (Note 27 g)	<b>(54)</b>	(28)	(14)
Capitalization of the integral result of financing (Note 27 h)	<b>(48)</b>	(44)	(25)
Derivative financial instruments (Note 27 i)		101	77
Deferred income taxes (Note 27 j)	<b>50</b>	142	544
Deferred employee profit sharing (Note 27 j)	<b>143</b>	240	106
Labor liabilities (Note 27 k)	<b>5</b>	(269)	(30)
Minority interest (Note 27 m)	<b>3</b>		(8)
Total U.S. GAAP adjustments	<b>98</b>	74	675
Net income under U.S. GAAP	<b>Ps. 6,720</b>	Ps. 5,840	Ps. 7,086

Under U.S. GAAP, the monetary position effect of the income statement adjustments is included in each adjustment, except for the capitalization of the integral result of financing, intangible assets and goodwill as well as pension plan liabilities, which are non-monetary.

**Table of Contents****b) Reconciliation of Stockholders' Equity:**

	2006	2005
Majority stockholders' equity under Mexican FRS	Ps. 54,220	Ps. 50,027
U.S. GAAP adjustments:		
Restatement of prior year financial statements		(238)
Participation in Coca-Cola FEMSA (Note 27 a)	(7)	(1)
Start-up expenses (Note 27 e)	(190)	(176)
Intangible assets and goodwill (Note 27 f)	52	52
Restatement of imported machinery and equipment (Note 27 g)	421	586
Capitalization of the integral result of financing (Note 27 h)	348	396
Deferred income taxes (Note 27 j)	497	120
Deferred employee profit sharing (Note 27 j)	(626)	(894)
Labor liabilities (Note 27 k)	(1,621)	(326)
Acquisition of Coca-Cola FEMSA minority interest	1,551	
Acquisition of Kaiser minority interest (Note 27 l)	77	
FEMSA's minority interest acquisition (Note 27 n)	16,524	16,524
<b>Total U.S. GAAP adjustments</b>	<b>17,026</b>	<b>16,043</b>
<b>Stockholders' equity under U.S. GAAP</b>	<b>Ps. 71,246</b>	<b>Ps. 66,070</b>

**c) Reconciliation of Comprehensive Income:**

	2006	2005	2004
Majority comprehensive income under Mexican FRS	Ps. 6,838	Ps. 4,254	Ps. 5,991
U.S. GAAP adjustments:			
Net income (Note 28 a)	98	74	675
Derivative financial instruments		325	115
Result of holding non-monetary assets	117	154	81
<b>Comprehensive income under U.S. GAAP</b>	<b>Ps. 7,053</b>	<b>Ps. 4,807</b>	<b>Ps. 6,862</b>

**Note 29. Future Impact of Recently Issued Accounting Standards Not Yet in Effect.****a) Mexican FRS:**

During 2006, the following new accounting standards were issued under Mexican FRS, the application of which is required as indicated. Except as noted below, the Company will adopt these standards as of January 1, 2007 and does not anticipate that these new standards will have a significant impact on its consolidated financial position or net income.

**Income Statement , or NIF B-3**

This standard sets the general standards for presenting and structuring the statement of income, the minimum content requirements and general disclosure standards. Consistent with NIF A-5, Basic Elements of Financial Statements, NIF B-3 now classifies revenues, costs and expenses, into ordinary and non-ordinary. Ordinary items (even if not frequent) are derived from the primary activities representing and entity's main source of revenues. Non-ordinary items are derived from activities other than those representing an entity's main source of revenues. Consequently, the classification of certain transactions as special or extraordinary, according to former Bulletin B-3, was eliminated. As part of the structure of the statement of income, ordinary items should be presented first and, at a minimum, present income or loss before income taxes,



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income or loss before discontinued operations, if any, and net income or loss. Presenting operating income is neither required nor prohibited by NIF B-3. Cost and expense items may be classified by function, by nature, or a combination of both. When classified by function, gross income may be presented. Statutory employee profit sharing should now be presented as an ordinary expense (within other income (expense) pursuant to NIF No. 4 issued in January 2007) and no longer presented with income tax. Special items mentioned in particular Mexican FRS should now be part of other income and expense and items formerly recognized as extraordinary should be part of non-ordinary items. NIF B-3 is effective for years beginning on January 1, 2007.

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**Table of Contents****Subsequent Events , or NIF B-13**

This standard requires that for (i) asset and liability restructurings and (ii) creditor waivers to their right to demand payment in case the entity defaults on contractual obligations, occurring in the period between the date of the financial statements and the date of their issuance, only disclosure needs to be included in a note to the financial statements while recognition of these items should take place in the financial statements of the period in which such events take place. Previously, these events were recognized in the financial statements instead in addition to their disclosure. NIF A-7, Presentation and Disclosure, in effect as of January 1, 2006, requires, among other things, that the date on which the issuance of the financial statements is authorized be disclosed as well as the name of authorizing management officer(s) or body (bodies). NIF B-13 establishes that if the entity owners or others are empowered to modify the financial statements, such fact should be disclosed. Subsequent approval of the financial statements by the stockholders or other body does not change the subsequent period, which ends when issuance of the financial statements is authorized. NIF B-13 is effective for years beginning on January 1, 2007.

**Related Parties , or NIF C-13**

This standard broadens the concept related parties to include a) the overall business in which the reporting entity participates; b) close family members of key officers; and c) any fund created in connection with a labor-related compensation plan. NIF C-13 requires the following disclosures: a) that the terms and conditions of consideration paid or received in transactions carried out between related parties are equivalent to those of similar transactions carried out between independent parties and the reporting entity, only if sufficient evidence exists; b) benefits granted to key officers; and c) name of the direct controlling company and, if different, name of the ultimate controlling company. Notes to comparative financial statements of prior periods should disclose the new provisions of NIF C-13. NIF C-13 is effective for years beginning on January 1, 2007.

**Capitalization of Integral Result of Financing , or NIF D-6**

This standard establishes general capitalization standards that include specific accounting for financing in domestic and foreign currencies or a combination of both. Some of these standards include: a) mandatory capitalization of integral result of financing ( RIF ) directly attributable to the acquisition of qualifying assets; b) in the instance financing in domestic currency is used to acquire assets, yields obtained from temporary investments before the capital expenditure is made are excluded from the amount capitalized; c) exchange gains or losses from foreign currency financing should be capitalized considering the valuation of associated hedging instruments, if any; d) a methodology to calculate capitalizable RIF relating to funds from generic financing; e) regarding land, RIF may be capitalized if development is taking place; and f) conditions that must be met to capitalize RIF, and rules indicating when RIF should no longer be capitalized. NIF D-6 is effective for years beginning on January 1, 2007.

**b) U.S. GAAP:**

The following new accounting standards have been issued under U.S. GAAP, the application of which is required as indicated. Except as noted below, the Company does not anticipate that those new standards will have a significant impact on its consolidated financial position or results of operations.

**Accounting for Certain Hybrid Financial Instruments an amendment of FAB Statement No. 133 and 140 , or SFAS No. 155**

This statement amends SFAS No.133, Accounting for Derivative Instruments and Hedging Activities, and No.140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. SFAS No. 133 establishes the following: a) permits fair value re-measurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, b) clarifies which interest-only strips and principal-only strips are not subject to SFAS No. 133 requirements, c) establishes requirements to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation, d) clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives, e) amends SFAS No. 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. This Statement is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The Company is in the process of determining the impact of adopting this new accounting principle on its consolidated financial position and results of operations.



**Table of Contents****Accounting for Servicing of Financial Assets – an amendment of FAB Statement No. 140 , or SFAS No. 156**

This statement amends SFAS No.140, with respect to the accounting for separately recognized servicing assets and servicing liabilities and establishes that entities must recognize servicing assets or servicing liabilities each time they undertake an obligation to service a financial asset by entering into a servicing contract in some specific situations. This Statement also requires recognizing separately servicing assets and servicing liabilities to be initially measured at fair value, if practicable; and also permits an entity to choose either the amortization method or the fair value measurement method to recognize servicing assets and servicing liabilities. This Statement is effective as of the beginning of first fiscal year that begins after September 15, 2006. The Company is in the process of determining the impact of adopting this new accounting principle on its consolidated financial position and results of operations.

**Fair Value Measurements , or SFAS No. 157**

This statement establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 clarifies the definition of exchange price as the price between market participants in an orderly transaction to sell an asset or transfer a liability in the market in which the reporting entity would transact for the asset or liability, that is, the principal or most advantageous market for the asset or liability. The changes to current practice resulting from the application of this statement relate to the definition of fair value, the methods used to measure fair value, and the expanded disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company is in the process of determining the impact of adopting this new accounting principle on its consolidated financial position and results of operations.

**Employers Accounting for Defined Benefit Pension and Other Postretirement Plans – an amendment of FASB Statements No. 87, 88, 106, and 132(R) , or SFAS No. 158**

This statement requires companies to (1) fully recognize, as an asset or liability, the over funded or under funded status of defined pension and other postretirement benefit plans; (2) recognize changes in the funded status through other comprehensive income in the year in which the changes occur; (3) measure the funded status of defined pension and other postretirement benefit plans as of the date of the company's fiscal year-end; and (4) provide enhanced disclosures. The provisions of this statement are effective for an employer with publicly traded equity securities, or controlled subsidiaries of such companies, in fiscal years ending after December 15, 2006. In addition, a company must now measure the fair value of its plan assets and benefit obligations as of the date of its year-end balance sheet. A company is no longer permitted to measure the funded status of its plan(s) by being able to choose a measurement date up to three months prior to year end. This provision within the standard is effective for all companies in fiscal years ending after December 15, 2008, however this provision does not impact the Company as its measurement date is the same as its fiscal year end. There is no impact on results of operations or cash flows. Retrospective application of this standard is not permitted. The impact of adopting the provisions of this statement that apply to the Company's December 31, 2006 consolidated financial statements is disclosed in Note 28.

**Accounting for Uncertainty in Income Taxes – an interpretation of FAB Statement No. 109, or SFAS Interpretation ( FIN ) No. 48**

This interpretation provides detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in a company's financial statements in accordance with SFAS No.109, Accounting for Income Taxes. FIN No. 48 requires a company to recognize the financial statement impact of a tax position when it is more likely than not that the position will be sustained upon examination. If the tax position meets the more-likely-than-not recognition threshold, the tax effect is recognized at the largest amount of the benefit that is greater than 50% likely of being realized upon ultimate settlement. Any difference between the tax position taken in the tax return and the tax position recognized in the financial statements using the criteria above results in the recognition of a liability in the financial statements for the unrecognized benefit. Similarly, if a tax position fails to meet the more-likely-than-not recognition threshold, the benefit taken in tax return will also result in the recognition of a liability in the financial statements for the full amount of the unrecognized benefit. FIN No. 48 will be effective for fiscal years beginning after December 15, 2006 (including the first interim period for calendar year companies) and the provisions of FIN No. 48 will be applied to all tax positions under SFAS No. 109 upon initial adoption. The cumulative effect of applying the provisions of this interpretation will be reported as an adjustment to the opening balance of retained earnings for that fiscal year. The Company is in the process of determining the impact of adopting this new accounting principle on its consolidated financial position and results of operations.

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**How Taxes Are Collected from Customers and Remitted to Governmental Authorities Should be Presented in the Income Statement , or EITF Issue No. 06-3**

The scope of this issue includes any tax assessed by a governmental authority that is directly imposed on a revenue-producing transaction between a seller and a customer and may include, but is not limited to, sales, use, value added, and some excise taxes. The Task Force reached a tentative conclusion that the presentation of taxes mentioned above on either a gross (included in revenues and costs) or a net (excluded from revenues) basis is an accounting policy decision that should be disclosed pursuant to Opinion 22. In addition, for any such taxes that are reported on a gross basis, a company should disclose the amounts of those taxes in interim and annual financial statements for each period for which an income statement is presented if those amounts are significant. The disclosure of those taxes can be done on an aggregate basis. This tentative conclusion requires only the presentation of additional disclosures, as a result an entity would not be required to reevaluate its existing policies related to taxes assessed by a governmental authority that are directly imposed on a revenue-producing transaction between a seller and a customer. However, if a company chooses to reevaluate its existing policies and elects to change the presentation of taxes within the scope of this Issue must follow the requirements of Statement No. 154, *Accounting Changes and Error Corrections* a replacement of APB Opinion No. 20 and FASB Statement No. 3. The Task Force also reached a tentative conclusion that this Issue should be applied to financial reports for interim and annual reporting periods beginning after December 15, 2006. Earlier application is permitted. The Company is in the process of determining the impact of adopting this new accounting principle on its consolidated financial position and results of operations.

**Note 30. Relevant Events.**

On December 19, 2006, Coca-Cola FEMSA and The Coca-Cola Company reached a definitive agreement to acquire Jugos del Valle, S.A.B. de C.V. ( Jugos del Valle ) in a transaction valued at \$470, including debt of \$90 as of December 31, 2006. Jugos del Valle produces and sells fruit juices, beverages and other fruit products. The Company is based in Mexico but markets its products internationally, particularly in Brazil and the United States.

On June 25, 2007, the Comisión Federal de Competencia of Mexico (CFC), or the Mexican Antitrust Commission, notified the Company of its decision to object to the acquisition of Jugos del Valle. The Company intend to consider our options, which may include seeking a reconsideration of the decision.

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**Report of Independent Registered Public Accounting Firm**

**To the Stockholders of**

**FEMSA COMERCIO, S.A. de C.V.**

We have audited the consolidated balance sheets of **FEMSA COMERCIO, S.A. de C.V. and Subsidiaries (a wholly-owned subsidiary of FOMENTO ECONÓMICO MEXICANO, S.A. de C.V.)** as of December 31, 2006 and 2005, and the related consolidated statements of income, stockholders' equity and changes in financial position for each of the three years in the period ended December 31, 2006 (not presented separately herein). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Mexico and in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of **FEMSA COMERCIO, S.A. de C.V. and Subsidiaries** at December 31, 2006 and 2005, and the consolidated results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 2006, in conformity with Mexican financial reporting standards, which differ in certain significant respects from accounting principles generally accepted in the United States of America, as described in Notes 20 and 21 to the consolidated financial statements.

**Mancera, S. C.,**

**A Member Practice of**

**Ernst & Young Global**

**/s/ Aldo Villarreal Robledo  
C.P.C. Aldo Villarreal Robledo**

San Pedro Garza García, N.L., Mexico

June 25, 2007