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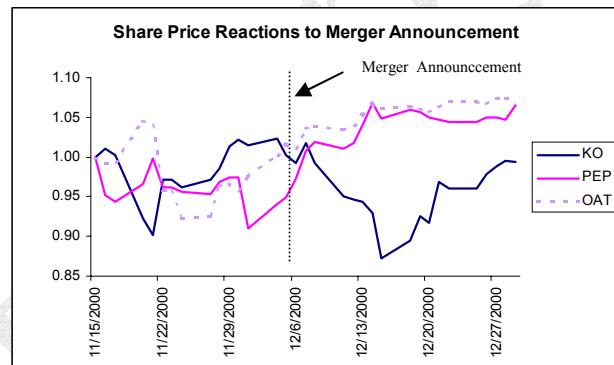
Coke vs. Pepsi, 2001

On December 4, 2000, PepsiCo, Inc. and The Quaker Oats Company issued a joint press release announcing their merger. The terms of the merger stated that PepsiCo would acquire Quaker Oats in a stock-for-stock deal valuing Quaker at around \$14 billion.

Judging by the share price reactions to the announcement, observers viewed the deal as yet another setback for Coca-Cola. By acquiring Quaker Oats, PepsiCo would gain access to Gatorade and control 83.6 percent of the sports-drink market. PepsiCo already possessed extremely strong brands in the non-carbonated beverages segment such as Aquafina, Tropicana and Lipton. Now through Gatorade, PepsiCo would consolidate its lead even further. Analysts estimated that PepsiCo would control around 33 percent of the United States' non-carbonated beverage market after the Gatorade acquisition, far ahead of Coca-Cola's 21 percent.¹ A report by UBS Warburg stated,

*"Given PEP's [PepsiCo's] #1 rank in the faster growth segment and its improving competitive position in CSD's [carbonated soft drinks], we believe PEP could, over the long term, threaten Coca-Cola's lead in the domestic beverage category in all channels except fountain."*²

Carolyn Keene, consumer analyst at the mutual fund firm Siegel, Parker and Lauck, (SPL) wondered how this latest announcement would affect the two companies' prospects for value creation. Historically, Coca-Cola had trounced PepsiCo in terms of value created as measured by "EVA"™ or Economic Value-Added (see **Exhibit 1**). She wondered if the trend would be reversed given recent developments. To develop a view, she decided to perform an



¹ "Deal Ensures Pepsi Outdistancing Coke on the Flat," South China Morning Post, December 6, 2000

² Caroline Levy, David Palmer and Elyse Sakowitz, "PepsiCo Inc.-Strong Buy", *UBS Warburg*, December 5, 2000

EVA analysis for Coca-Cola Co. and PepsiCo for 2001-2003. She hoped this would reveal which of the two companies would be the more attractive investment over the next few years.

Company Background: The Coca-Cola Company

In 2000, The Coca-Cola Company's (ticker symbol: KO) annual sales were \$20.5 billion, and its market value reached \$110.1 billion. The company was the largest manufacturer, distributor and marketer of soft drink concentrates and syrups³ in the world, and also marketed and distributed a variety of non-carbonated beverage products, which included Minute Maid orange juice, Fruitopia, Dasani bottled water, and Nestea among others.

From 1993 to 1998, The Coca-Cola Company had consistently garnered the first or second spot in *Fortune*'s annual ranking of the top wealth creators. One of the main reasons for this was the company's strategy of spinning off its bottling operations in order to avoid consolidation on its balance sheet. This move, implemented in 1985, contributed to a dramatic rise in returns on equity from 23 percent to as much as 57 percent over the last two decades (see **Exhibit 2**).

Recently however, the company had run into difficulties. The Asian financial crisis, South America's difficulties, and Russia's devaluation of the ruble all hurt KO. But business mistakes by Doug Ivester, CEO from 1997 to 1999, aggravated the situation.

An example of one such mistake occurred in November 1999, when Ivester instituted a 7.7 percent price hike on syrup, a rate that was double that of usual increases. The Coca-Cola Company's bottlers were infuriated, and felt that Ivester was gouging them in order to increase KO's profits. In response, the bottlers raised prices for the first time in years in order to improve profitability, resulting in a decrease in volume (see **Exhibit 3**). During Ivester's approximately two-year term, net income fell by 41 percent. The company's board of directors eased Ivester out in December 2000.

Douglas Daft, head of Coca-Cola's Middle and Far East, and Africa groups, was chosen to succeed Ivester. Upon taking over he immediately instituted major organizational changes such as cutting staff and reducing bureaucracy. But perhaps the most important change was his acknowledgment that KO needed to be a dominant player in the noncarbonated beverages market. In contrast to Ivester who had insisted on pushing the company's core soft drink brands

³ The Coca Cola Company did not actually bottle and distribute its soft drink products. Rather, the company manufactured concentrate and syrups that were then sold to authorized bottlers who were either majority or minority owned by KO, or completely independent. These bottlers then combined the syrup or concentrate with carbonated water and sweetener, packaged the finished drinks in authorized containers bearing the Coca-Cola trademark, and then sold these to retailers and wholesalers. Thus, KO's main source of profit was from the syrup.

– Coca-Cola, Fanta, Sprite and Diet Coke – Daft and his executives worked hard to come up with new noncarbonated products.

Some analysts were optimistic that the change in management would return The Coca-Cola Company to its glory days. Perhaps through improved relations with bottlers and acquisitions of non-carbonated beverages, KO would return to the profit margins before 1998. Other analysts were less enthusiastic. One thing was certain, however: with PepsiCo's invigorated management, KO would need to get back on its feet as quickly as it could.

Company Background: PepsiCo, Inc.

In 2000, PepsiCo, Inc. was a \$20 billion dollar company involved in the snack food, soft drink and noncarbonated beverage businesses. The company sold and distributed salty and sweet snacks under the Frito-Lay trademark, and manufactured concentrates of Pepsi, Mountain Dew and other brands for sale to franchised bottlers. The company also produced and distributed juices and other noncarbonated beverages.⁴ Snack foods accounted for roughly two-thirds of PepsiCo's sales and operating income, while beverages accounted for the remainder.

PepsiCo as a focused snack and beverage company in 2000 was due mostly to the efforts of Roger Enrico, CEO from 1996 to 2000. During his tenure, Enrico instituted a massive overhaul at PepsiCo. In 1997, he sold off the fast food chains KFC, Taco Bell and Pizza Hut, ridding PepsiCo of a business that had long been a drag on returns. In 1999, he spun off Pepsi's capital-intensive bottling operations into an independent public company. By spinning off the bottling operations PepsiCo would be left with just the higher-margin business of selling concentrate to bottlers.⁵ At the same time, independent PepsiCo bottlers would be able to raise capital on their own, freeing up cash flow within the parent company for other uses. Enrico also took aggressive steps to make PepsiCo a "total beverage company". He brokered the acquisitions of Tropicana, the market leader in orange juice, and Quaker Oats, whose Gatorade brand dominated the energy drink market.

During Enrico's term, PepsiCo's return on equity almost doubled from 17 percent in 1996 to 30 percent in 2000. (See **Exhibit 2** for historical returns and **Exhibit 1** for a historical EVA analysis.) On Wall Street, analysts were upbeat about PepsiCo's prospects.

⁴ Yahoo Finance.

⁵ In a price war "it's the bottlers' margins that get flattened, while the "parent" companies enjoy higher sales volume because of the low prices. The concentrate business...can have gross margins of 80%, compared with between 35% and 40% for bottling." --Nikhil Deogun, "PepsiCo's Sale of Bottling-Business Stake Isn't Being Greeted With "dot com" Hype", *The Wall Street Journal*, March 26, 1999, p. C1.

Industry Overview and Competitive Events

In 2000, the beverage industry was undergoing a rapid transformation: the non-carbonated drinks segment, although still representing only a small fraction of the beverage market, had grown by 62 percent in volume over the last five years, while soft drink volume growth had been sluggish.⁶ According to Beverage Digest, the share of the carbonated soft-drink industry fell from 71.3 percent in 1990 to 60.5 percent in 2000.

In soft drink volume, PepsiCo still lagged behind Coke, although it seemed to have caught up somewhat in recent years (see **Exhibit 3**). In the fall of 1999 for instance, PepsiCo, for the first time in its history, occupied two of the top three places for U.S. soft drink brands on store shelves as its Mountain Dew dislodged Diet Coke from third place.⁷

Recent developments at both companies signaled an aggressive new round of competition. Below is a summary of recent competitive moves by both companies in several beverage categories:

Soft Drinks

Over the last five years, Pepsi had launched aggressive and exciting marketing campaigns (e.g. “Generation Next”, “Joy of Pepsi”) that helped boost volumes and visibility. In addition, Pepsi launched the “Power of One” campaign – a strategy that entailed moving Pepsi drinks next to Frito-Lay on store shelves on the bet that doing so would entice shoppers to pick up a Pepsi when they bought chips. This strategy also helped boost both Frito Lay’s and Pepsi’s volumes. In response to the success of the Pepsi campaigns, Coca-Cola resorted to a number of tactics, such as veering away from its traditional feel-good ads and launching more trendy ones in the summer of 2000. Unfortunately, the new ads were highly unpopular and elicited negative reactions from customers and bottlers.⁸ Coca-Cola pulled out the ads and replaced them with the “Life tastes good” series, which returned to Coke’s traditional ‘feel-good’ themes while being trendier at the same time.

Non Carbonated Beverages

Coke and PepsiCo raced to position themselves in this important and fast-growing market segment:

- **Orange Juice.** PepsiCo acquired Tropicana in 1998 and claimed the clear market leader in orange juice. Tropicana held over 40 percent of the total chilled orange juice market, and 70 percent of the not-from-concentrate

⁶ McCarthy, “Buffeted: Coke’s Muddle over Quaker”, *The Economist*, November 25, 2000

⁷ Byrne, John A., “PepsiCo’s New Formula: How Roger Enrico Is Remaking the Company,” *Business Week*, April 10, 2000

⁸ The ads were produced by the Cliff Freeman Ad Agency, famous for its controversial dot-com ad in which gerbils are being shot out of a cannon. One example of a Coke commercial featured a grandmother in a wheelchair who throws a tantrum when she discovers there is no Coke at a family reunion.

orange juice segment in the United States. On the other hand, Coke's Minute Maid had less than a 20 percent share of the chilled orange juice market.

- **Bottled Water.** PepsiCo test-marketed Aquafina as early as 1994, while Coke did not enter the bottled water market until 1999 with its Dasani brand. Aquafina was the number one brand in the US market for bottled water in 2000.
- **Iced Tea.** In iced-tea, PepsiCo's Lipton boasted a 16-point share lead over Coca-Cola's Nestea.
- **Sports Drinks.** Pending the Federal Trade Commission's approval of the PepsiCo-Quaker Oats deal, PepsiCo would own Gatorade, which held 83 percent of the US sports-drink market. Coca-Cola's Powerade was a far second at 11 percent.
- **Specialty Drinks.** PepsiCo, in alliance with Starbucks, introduced the highly popular Starbucks Frappuccino in 1996. It took Coca-Cola until 2000 to announce that it was going to test market a frozen coffee beverage. In October 2000, PepsiCo beat Coca-Cola in acquiring South Beach Beverage Co., maker of SoBe brand of teas and fruit juices.

Financial Comparison

Analysts expected that the coming months would be among the most exciting in the Coke-Pepsi saga. It would be interesting to see how the revived 'cola wars' would play out. In the meantime, a look at some performance measures might provide clues as to what the future held:

- *Ratio analysis.* **Exhibits 4 and 5** present a variety of analytical ratios computed from the financial statements of each firm.
- *Economic Profit Analysis.* Also known as "Economic Value Added," EVA sought to estimate the value created or destroyed by comparing a firm's cash operating profits or "Net Operating Profits After Tax" (NOPAT) against a capital charge:

$$\text{EVA} = \text{NOPAT} - (\text{Weighted Average Cost of Capital} \times \text{Invested Capital})$$

Alternatively, the formula could be written as:

$$\text{EVA} = (\text{Return on Invested Capital, ROIC} - \text{WACC}) \times \text{Invested Capital}$$

Return on Invested Capital, as the name suggested, could be calculated by dividing NOPAT by Invested Capital. The second formula highlights the idea that a “spread” earned beyond a company’s cost of capital resulted in value creation.

Conclusion

Coke and Pepsi had created one of the strongest rivalries in business history. Carolyn Keene now wanted to develop a view about the two companies’ future performances. She obtained projections pro-forma for the two firms from reports prepared by analysts at Credit Suisse First Boston⁹ (see **Exhibits 6 and 7**), and gathered information about current capital market conditions (**Exhibit 8**). She also took out her guidelines for estimating the components of EVA (**Exhibit 9**). It would be nice to finish her analysis before going off for Christmas break.

⁹ KO forecasts were obtained from report entitled “Third Quarter Review of 10Q: Flat Revenue and Varied Operating Performance” by Andrew Conway, Chris O’ Donnell and Corey Horsch, *Credit Suisse First Boston Equity Research*, November 19, 2001. PepsiCo forecasts were obtained from report entitled “A Balanced Formula for Growth” by Andrew Conway, Chris O’ Donnell and Corey Horsch, *Credit Suisse First Boston Equity Research*, November 8, 2001.

Exhibit 1

Coke vs. Pepsi, 2001

**Historical EVA™ Estimation and Return Comparisons
Coca-Cola Co. and PepsiCo, Inc.**

The Coca-Cola Company

(\$MM)	1994	1995	1996	1997	1998	1999	2000
NOPAT	2,547	2,783	2,583	3,381	3,178	2,605	2,349
Invested capital	7,769	8,466	9,649	13,825	15,896	15,644	15,864
Return on invested capital	32.8%	32.9%	26.8%	24.5%	20.0%	16.6%	14.8%
WACC	12.2%	11.4%	13.4%	12.9%	11.1%	9.9%	8.4%
ROIC-WACC Spread	20.6%	21.4%	13.4%	11.6%	8.9%	6.8%	6.4%
EVA	1,602	1,814	1,292	1,601	1,422	1,063	1,016

PepsiCo, Inc.

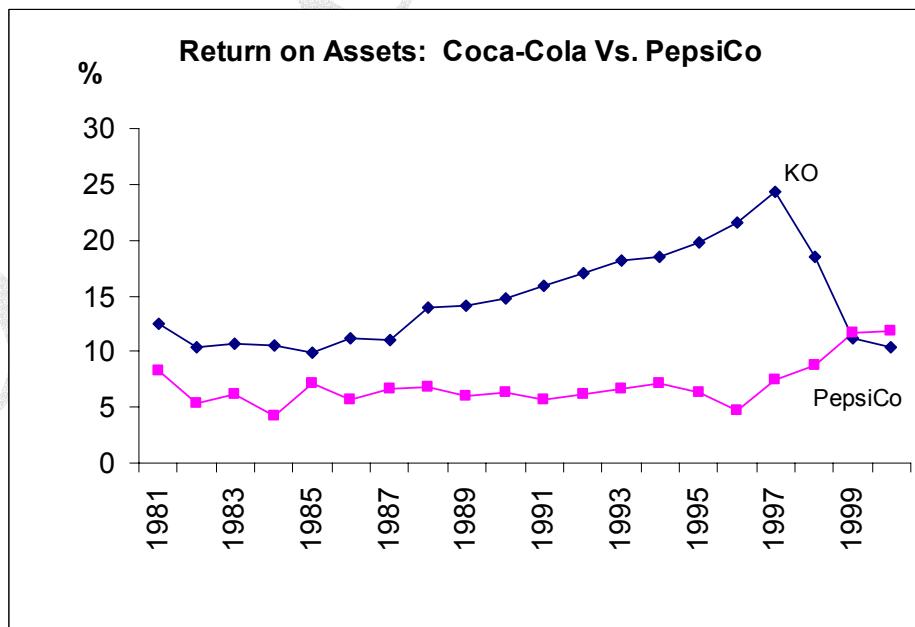
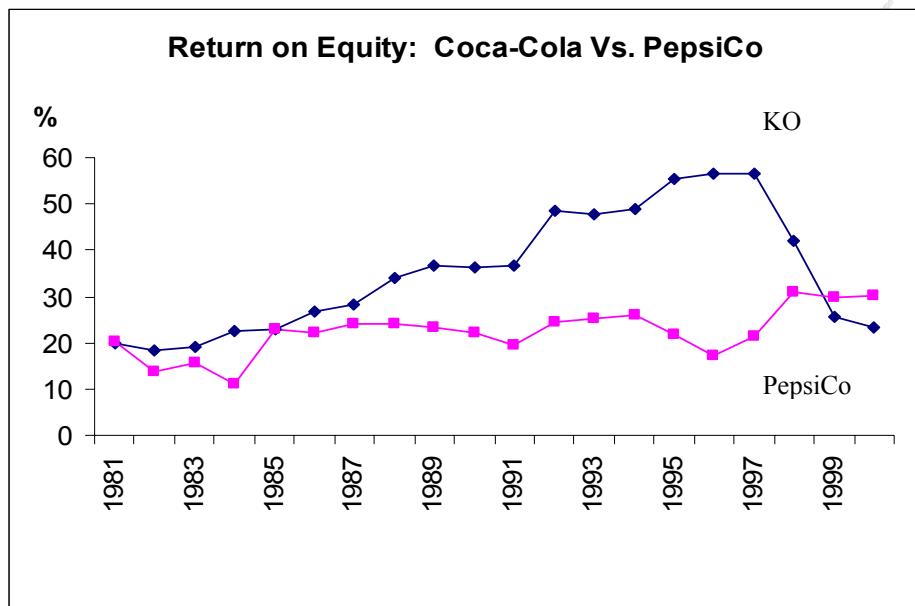
(\$MM)	1994	1995	1996	1997	1998	1999	2000
NOPAT	2,122	2,204	1,892	1,922	2,522	1,794	2,292
Invested capital	22,507	27,009	26,823	16,392	19,439	12,849	13,146
Return on invested capital	9.4%	8.2%	7.1%	11.7%	13.0%	14.0%	17.4%
WACC	11.5%	11.0%	10.5%	11.6%	10.8%	9.9%	8.3%
ROIC-WACC Spread	-2.1%	-2.8%	-3.4%	0.1%	2.2%	4.1%	9.1%
EVA	(464)	(760)	(916)	24	428	522	1,201

Source: Casewriter estimates.

Exhibit 2

Coke vs. Pepsi, 2001

Return on Equity and Return on Asset Comparisons, Coca-Cola and PepsiCo



Source: casewriter estimates

Exhibit 3

Coke vs. Pepsi, 2001

U.S. Soft Drink Market Shares and Volume, Coca-Cola and PepsiCo

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Coca-Cola											
Gallonage (in millions)	4,915.5	5,038.4	5,108.9	5,310.0	5,580.8	5,915.4	6,223.9	6,473.0	6,764.4	6,730.5	6,737.2
Growth	4.0%	2.5%	1.4%	3.9%	5.1%	6.0%	5.2%	4.0%	4.5%	-0.5%	0.1%
Market share	41.0%	41.3%	41.3%	41.7%	42.0%	42.9%	43.8%	44.1%	44.6%	44.1%	44.0%
Market share gain/(loss)	0.6%	0.3%	0.0%	0.4%	0.3%	0.9%	0.9%	0.3%	0.5%	-0.5%	-0.1%
PepsiCo											
Gallonage (in millions)	3,970.5	4,010.2	3,827.6	3,899.0	4,070.6	4,201.8	4,370.2	4,500.2	4,704.1	4,732.3	4,736.1
Growth	3.0%	1.0%	-4.6%	1.9%	4.4%	3.2%	4.0%	3.0%	4.5%	0.6%	0.1%
Market share	33.1%	32.9%	30.9%	30.6%	30.7%	30.6%	30.8%	30.7%	31.0%	31.0%	30.9%
Market share gain/(loss)	0.1%	-0.2%	-2.0%	-0.3%	0.1%	-0.1%	0.2%	-0.1%	0.3%	0.0%	-0.1%
Soft Drink Industry											
Gallonage (in millions)	11,996.1	12,200.4	12,473.2	12,722.7	13,275.0	13,752.9	14,199.5	14,665.8	15,160.6	15,251.6	15,328.0
Growth	2.6%	1.7%	2.2%	2.0%	4.3%	3.6%	3.2%	3.3%	3.4%	0.6%	0.5%

Source: Compiled from Beverage World

Exhibit 4

Coke vs. Pepsi, 2001

Analytical Financial Ratios, The Coca-Cola Company

	1994	1995	1996	1997	1998	1999	2000
Activity Analysis							
Average days outstanding	31.24	32.61	32.83	31.73	32.06	31.92	31.71
Working capital turnover	(16.33)	(11.27)	(10.62)	(8.90)	(6.14)	(5.49)	(6.52)
Fixed assets turnover	3.59	3.60	3.87	4.33	4.36	3.79	3.32
Total asset turnover	1.08	1.12	1.15	1.12	1.05	0.92	0.93
Liquidity Analysis							
Current ratio	0.64	0.59	0.80	0.75	0.87	0.90	0.87
Cash ratio	0.25	0.18	0.22	0.21	0.18	0.18	0.20
Cash from operations ratio	0.54	0.45	0.47	0.47	0.35	0.39	0.38
Long Term Debt and Solvency Analysis							
Debt equity ratio	0.67	0.75	0.73	0.61	0.65	0.65	0.61
Times interest earned	18.63	14.80	13.69	19.38	17.93	11.82	8.26
Fixed charge coverage ratio	10.02	9.87	7.18	8.99	8.70	6.03	5.77
Capital expenditure ratio	3.83	3.55	3.50	3.69	3.98	3.63	4.89
Cash from operations-debt ratio	0.96	0.82	0.77	0.78	0.55	0.62	0.63
Profitability Analysis							
Operating margin	22.9%	22.3%	21.1%	26.5%	26.4%	20.1%	18.0%
Net profit margin	15.8%	16.6%	18.8%	21.9%	18.8%	12.3%	10.6%
ROA	16.8%	17.7%	19.1%	21.1%	22.9%	17.3%	11.5%
ROE	44.3%	48.1%	51.7%	48.0%	46.1%	37.1%	25.8%
Financial leverage effect*	70.1%	68.9%	74.2%	89.2%	82.6%	71.1%	61.0%
Growth							
Sales	15.9%	11.4%	2.9%	1.7%	-0.3%	5.3%	3.3%
Book assets	15.4%	8.4%	7.4%	4.5%	13.4%	12.9%	-3.6%
Net income before unusual gain/loss	16.7%	16.9%	16.9%	18.2%	-14.4%	-31.2%	-10.4%
Adjusted NOPAT	19.5%	8.6%	-2.8%	27.7%	-0.7%	-19.8%	-7.3%
Net income	17.4%	16.9%	16.9%	18.2%	-14.4%	-31.2%	-10.4%
Operating income	19.5%	8.6%	-2.8%	27.7%	-0.7%	-19.8%	-7.3%

*Net income/operating income

Source: Company 10-K Filings with SEC

Exhibit 5

Coke vs. Pepsi, 2001

Analytical Financial Ratios, PepsiCo, Inc.

	1994	1995	1996	1997	1998	1999	2000
Activity Analysis							
Average days outstanding	25.33	26.89	28.39	40.71	37.59	37.25	31.28
Working capital turnover	(34.07)	513.67	200.28	20.98	(28.69)	(12.86)	38.78
Fixed assets turnover	1.64	1.72	1.82	1.42	1.57	1.55	2.05
Total asset turnover	1.17	1.20	1.27	0.94	1.05	1.01	1.14
Liquidity Analysis							
Current ratio	0.96	1.06	1.00	1.47	0.55	1.10	1.17
Cash ratio	0.28	0.29	0.15	0.68	0.05	0.28	0.34
Cash from operations ratio	0.71	0.72	0.82	0.80	0.41	0.80	0.99
Long Term Debt and Solvency Analysis							
Debt equity ratio	1.39	1.73	1.97	0.71	1.24	0.44	0.33
Times interest earned	4.96	4.38	4.24	5.57	6.54	7.76	14.59
Fixed charge coverage ratio	3.03	2.72	2.48	3.41	3.09	3.73	4.36
Capital expenditure ratio	1.65	1.78	1.83	2.27	2.29	2.71	3.67
Cash from operations-debt ratio	0.39	0.30	0.32	0.69	0.40	0.99	1.62
Profitability Analysis							
Operating margin	11.3%	9.9%	8.0%	12.7%	11.6%	13.8%	15.8%
Net profit margin	6.2%	5.3%	3.6%	10.2%	8.9%	10.1%	10.7%
ROA	7.2%	6.4%	4.6%	9.6%	9.3%	10.2%	12.2%
ROE	24.1%	24.7%	23.0%	16.9%	32.1%	30.0%	29.0%
Financial leverage effect*	54.6%	54.7%	53.8%	45.1%	80.5%	77.1%	72.7%
Growth							
Sales	13.3%	6.7%	4.6%	-33.9%	6.8%	-8.9%	0.3%
Book assets	4.6%	2.6%	-3.6%	-18.0%	12.7%	-22.5%	4.5%
Net income before unusual gain/loss	12.3%	-10.0%	-28.5%	29.8%	33.7%	2.9%	6.5%
Adjusted NOPAT	10.1%	-6.7%	-14.8%	4.6%	-2.9%	9.1%	14.4%
Net income	10.3%	-8.3%	-28.5%	86.4%	-7.0%	2.9%	6.5%
Operating income	10.1%	-6.7%	-14.8%	4.6%	-2.9%	9.1%	14.4%

*Net income/operating income

Source: Company 10-K Filings with SEC

Exhibit 6

Coke vs. Pepsi, 2001

Income Statement and Balance Sheet Forecasts, Coca-Cola Co.

Income Statement	2001E	2002E	2003E	Balance Sheet	2001E	2002E	2003E
Net operating revenue	20,223	21,234	22,508	Cash & equivalents	2,238	2,406	2,432
Cost of goods sold	6,092	6,285	6,617	A/R, Net	1,838	1,930	2,046
Gross profit	14,131	14,949	15,891	Inventories	1,015	1,048	1,103
Selling expense	7,508	7,569	7,985	Prepaid expenses & other	1,834	1,868	1,964
General & admin.	1,224	1,248	1,273	Total current assets	6,925	7,252	7,545
	8,732	8,817	9,258	Investments in bottlers	5,962	6,189	6,449
Operating income	5,399	6,132	6,633	Marketable securities	2,364	2,364	2,364
Interest income	295	244	254	PP&E	7,334	8,084	8,834
Interest expense	(310)	(280)	(264)	Less: Acc. depreciation	(2,935)	(3,476)	(4,073)
Equity income	197	227	261	Net PP&E	4,399	4,608	4,761
Other income/(deductions), net	24	(10)	(10)	Goodwill & other	1,783	1,488	1,193
Pretax Income	5,605	6,313	6,874	Total assets	21,434	21,901	22,311
Income Taxes	1,682	1,894	2,062	A/P & accrued liabilities	3,796	3,868	4,066
Net Income	3,923	4,419	4,812	Loans and notes payable	3,600	3,500	3,400
Supplemental Information:				Current portion of long-term debt	154	153	2
Depreciation	489	542	597	Accrued income taxes	643	724	788
Amortization	295	295	295	Total current liabilities	8,193	8,245	8,256
Cash taxes	1,738	1,957	2,131	Long-term debt	681	528	526
Capital expenditures	700	750	750	Other	991	991	991
Accumulated goodwill amortization at the end of 2000 was expected to be \$192 million.				Deferred income taxes	302	239	170
The reader should assume net income reflects the deduction of depreciation and amortization.				Total liabilities	10,167	10,003	9,943
				Common stock	870	870	870
				Additional paid-in capital	3,196	3,196	3,196
				Retained earnings	23,466	26,097	29,067
				Accumulated other comprehensive losses	(2,722)	(2,722)	(2,722)
				Treasury stock	(13,543)	(15,543)	(18,043)
				Total equity	11,267	11,898	12,368
				Total liabilities and equity	21,434	21,901	22,311

Source (except for accum. goodwill amortization): "Third Quarter Review of 10Q: Flat Revenue and Varied Operating Performance" by Andrew Conway, Chris O' Donnell and Corey Horsch, *Credit Suisse First Boston Equity Research*, November 19, 2001.

Exhibit 7

Coke vs. Pepsi, 2001

Income Statement and Balance Sheet Forecasts, PepsiCo, Inc.

Income Statement	2001E	2002E	2003E	Balance Sheet	2001E	2002E	2003E
Revenues				Cash	1,775	3,677	2,457
Beverages	10,553	11,307	12,116	Investments	466	466	466
Frito-Lay	14,498	15,373	16,273	Cash and equivalents	2,241	4,143	2,923
Quaker Foods	2,042	2,109	2,179	A/R, Net	2,292	2,435	2,585
	27,093	28,789	30,568	Inventories	1,284	1,364	1,449
Operating Profit				Prepaid Exp. & Other	886	942	1,000
Beverages	1,667	1,818	1,976	Total non-cash current assets	4,462	4,741	5,034
Frito-Lay	2,675	2,955	3,239	PP&E	7,449	8,021	8,493
Quaker Foods	408	426	446	Intangibles	4,556	4,556	4,556
Synergies	-	60	90	Investments in unconsol. affiliated	3,095	3,235	3,414
Corporate expense	(365)	(374)	(382)	Other	952	1,019	1,090
	4,385	4,885	5,369	Total assets	22,757	25,716	25,511
Net interest expense	148	92	37	Short-term borrowings	202	-	-
Equity income	157	186	239	Current portion of long term debt	281	444	64
Pretax Income	4,394	4,979	5,571	Accts payable & other current liabs	5,017	5,284	5,573
Provision for taxes	1,406	1,593	1,783	Total current liabilities	5,500	5,728	5,637
Net income	2,988	3,386	3,788	Long term debt	2,106	1,825	1,381
				Other liabilities	4,244	4,541	4,859
Supplemental information:				Deferred income taxes	1,625	1,974	2,252
Depreciation	900	950	1,000	Total liabilities	13,475	14,068	14,129
Amortization	236	295	295	Preferred stock			
Cash taxes	1,142	1,245	1,504	Common stock & add'l paid-in capital	690	690	690
Capital expenditures	1,860	1,583	1,528	Retained earnings	18,420	20,786	23,520
				Treasury stock	(8,434)	(8,434)	(11,434)
Accumulated goodwill amortization at the end of 2000 was expected to be \$751 million.				Accumulated comprehensive loss	(1,394)	(1,394)	(1,394)
The reader should assume net income reflects the deduction of depreciation and amortization.				Total equity	9,282	11,648	11,382
				Total liabilities and equity	22,757	25,716	25,511

Source (except for depreciation, amortization, and accum. goodwill amortization): "A Balanced Formula for Growth" by Andrew Conway, Chris O' Donnell and Corey Horsch, *Credit Suisse First Boston Equity Research*, November 8, 2001.

Exhibit 8

Coke vs. Pepsi, 2001

Capital Market Information On December 4, 2000

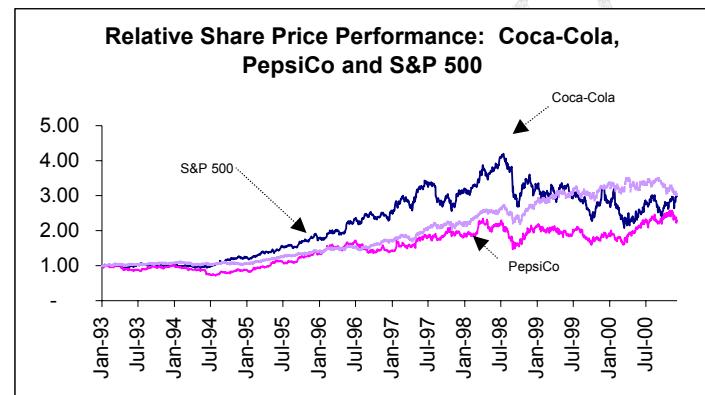
Coca-Cola Co. and PepsiCo Inc. Share Price Performance Relative to S&P500:
January 1993 to December 4, 2000

Current yields on U.S. Treasuries

3-month	6.15%
6-month	6.11%
1-year	6.00%
5-year	5.52%
10-year	5.73%
20-year	5.82%

Historical Equity Risk Premiums (1926-1999)

Geometric mean	5.90%
Arithmetic mean	7.50%



The Coca-Cola Company	
<u>Publicly Traded Debt*</u>	
Coupon	5.75% paid semi-annually
Maturity	4/30/2009
Current Price	91.54
Rating	A1
<u>Historic Betas</u>	
1994	0.88
1995	0.83
1996	1.19
1997	1.11
1998	0.97
1999	0.71
2000	0.44
Average	0.88
<u>Dividend History and Forecasts</u>	
Paymt Dates	31-Mar 30-Jun 30-Sep 31-Dec Total
1996	- 0.125 0.125 0.25 0.50
1997	- 0.14 0.14 0.28 0.56
1998	- 0.15 0.15 0.30 0.60
1999	- 0.16 0.16 0.32 0.64
2000	- 0.17 0.17 0.34 E 0.68
E=estimate	
Value Line Forecast of Dividend Growth from '97-99 to '03-'05:	
7.50%	
Value Line EPS Estimate for FY 2001:	
\$ 1.75	
Coke share price on December 4, 2000:	
\$ 62.75	
Outstanding shares (in millions):	
Basic	2,477
Diluted	2,487

PepsiCo, Inc	
Coupon	5.75% paid semi-annually
Maturity	1/15/2008
Current Price	93.26
Rating	A2
<u>Historic Betas</u>	
1994	1.05
1995	1.07
1996	0.93
1997	0.96
1998	1.03
1999	0.73
2000	0.42
Average	0.88
<u>Dividend History and Forecasts</u>	
Paymt Dates	31-Mar 30-Jun 30-Sep 31-Dec Total
1996	0.20 0.115 0.115 - 0.43
1997	0.23 0.125 0.125 - 0.48
1998	0.25 0.13 0.13 - 0.51
1999	0.26 0.135 0.135 - 0.53
2000	0.27 0.14 0.14 - 0.55
Value Line Forecast of Dividend Growth from '97-99 to '03-'05:	
7.50%	
Value Line EPS Estimate for FY 2001:	
\$ 1.63	
PepsiCo share price on December 4, 2000:	
\$ 43.81	
Outstanding shares (in millions):	
Basic	1,446
Diluted	1,475

Exhibit 12

Coke vs. Pepsi, 2001

Some Guidelines for Estimating Components of EVA

- **NOPAT.** “Net operating profit after taxes” (NOPAT) is calculated with the aim of arriving at the actual cash generated by the concern. Adjustments might include adding back goodwill amortization and other non-cash expenses. Taxes must similarly be adjusted to reflect only actual cash taxes. Depreciation is not added back to NOPAT despite being a non-cash expense, because of the assumption that depreciation represents a true economic cost, i.e. it is the amount that must be reinvested to maintain operations at the existing level. For consistency, invested capital is measured net of depreciation.
- **Invested Capital.** Invested capital means simply, the amount of capital invested in the business. It may be calculated either from the asset side, or from the liabilities + equity side of the balance sheet. The latter is the simpler method.

Invested capital includes debt, equity and other near-capital items that represent economic value employed on behalf of the firm such as the present value of operating leases, write-offs and cumulative losses, and accumulated goodwill amortization. The rationale for including losses and write-offs in continuing capital is that these represent unproductive assets, or failed investment. Were they excluded from the capital equation, the sum would only count successful efforts, and not accurately reflect the performance of the firm. Accumulated goodwill amortization likewise needs to be included in invested capital because it represents a true investment. Excess cash not needed for operations, such as marketable securities, may be deducted from the invested capital base.

- **Cost of capital.** The capital charge applied against NOPAT should be based on a blend of the costs of all the types of capital the firm employs, or the weighted average cost of capital.

$$WACC = K_d (1-t) * D/(D+E) + K_e * E/(D+E)$$

Where:

K_d	=	Cost of debt
T	=	Effective marginal tax rate
K_e	=	Cost of equity
D	=	Total debt
E	=	Total equity

The cost of debt (used for both debt and leases) is the annual rate consistent with each firm's bond rating. The cost of equity may be estimated in a variety of ways¹⁰—a usual practice is to use the capital asset pricing model:

$$K_e = R_f + \beta (R_m - R_f)$$

where:

R_f = Risk-free rate, typically the yield on 10-year US Treasury bonds
 β = Beta, a measure of the volatility of a company's stock price with respect to market movements
 $R_m - R_f$ = Market risk premium, the additional return investors require over the risk free rate to compensate them for investing in companies.¹¹

¹⁰ Other ways of estimating the cost of equity include the dividend growth and earnings capitalization models.

¹¹ The two market premiums frequently used are 7.5 percent, which is an arithmetic average of annual market returns over the Treasury-bill rate from 1926-1998, and 5.9 percent, which is a compound or geometric average of market returns over Treasury bonds from 1926-1998. (Source: *Ibbotson Associates Yearbook, 1999*)



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