ILLINOIS

Taste the feeling… Should you?

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The Coca-Cola company is the world's largest beverage company with 20-billion-dollar brands with operations in the entire world except Cuba and N. Korea. The company produces the concentrate for the soft drink and sells it to various bottlers worldwide. It has an estimated 1.8 billion beverage servings each day. Coca-Cola is the flagship brand of 'The Coca-Cola Company'. While there are many other soda brands viz. Diet Coke, Coca-Cola Zero, Fanta, Sprite etc. and other types of products owned by 'The Coca-Cola Company', this article will concentrate on Coca-Cola that amounts to 78% of the total soda sales. Coca-Cola is a non-alcoholic carbonated soft drink and one of the world's most valuable and recognized brands.[1][2]

The total revenue of 'The Coca-Cola Company' was $43.25 Billion in the last 12 months. 84% of this revenue comes from the sales of soft drink concentrate, while about 15% comes from their bottling operations.[bloomberg] About 70% of total revenue is generated just by the soft drink segment. While the company has its businesses globally, North America contributes 49.2% of the revenue. To increase its businesses outside North America, the company undertook many mergers and acquisitions (M&As). Major recent M&As include, a 16.7% stake in Monster Beverage Corporation and about 17% stake in Keurig Green Mountain.

It favors Coca Cola that every human is a potential consumer of the product, however soda has a higher consumption among young people than the older ones. Thus an increase in working population directly translates to an increase in demand. Coca Cola increased its prices by 3% in early the 2015 which helped boost its revenues by 1.3%. The sales during this period decreased by 1.6%[3], however the decrease in sales can be attributed to people making healthier choices rather than the price hike. It is practical to say that the demand for Coca Cola is quite inelastic at its current price. Seasonality of the demand is apparent in the annual trends of stock prices with a consistent high performance in the second quarter. The summer season increases the consumption of cold drinks, and this boost is pushed by the fact that a huge chunk of young people is on vacations. Some non-conventional factors can also affect its demand, e.g. the Arab Ban on Coca Cola till the 1990s.

Tie-ups with restaurants has been an important component of the sales. Although Coca Cola is a normal good, mutual agreements with inferior brands such as McDonalds can help Coca Cola hedge against recession. All so, because people would increase their consumption of the inferior complements during an economic downturn. While the archrival Pepsi lost 5.5% of its sales because of the recession of 2008, Coca Cola lost only 4% of its sales.

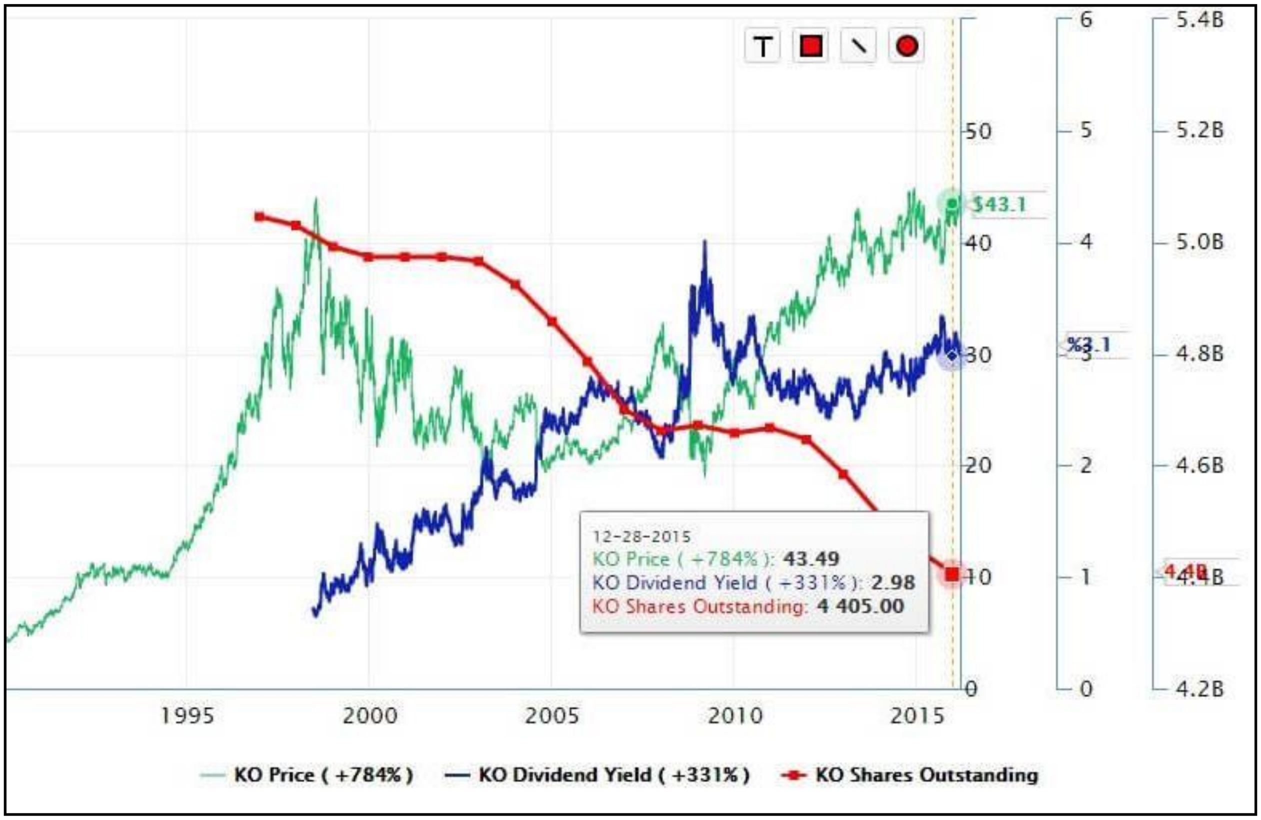
The market for soda appears to resemble a mixture of monopolistic competition (locally) and oligopoly (globally). There are no difficult barriers to entry on a small scale, but a very few firms have the majority of global market share owing to an early bird bonus. Such a market has kept the small local firms as price takers, whereas the giants do not enjoy a great pricing power either. The product differentiation of these big giants drive the entire market. Just as launch of new products by Coca Cola affects its demand, a new product launched by its rivals also affects the demand of Coca Cola. Thus resulting in a movement of its consumer base. The companies also rely heavily on their expensive marketing strategies -including advertising and sponsorship deals with major sporting events or teams- to boost their consumption and hence the demand for their product cannot be mapped solely to the quality of the product.

Source: http://: http://promotedifferent.com/pepsi-vs-cocacola-halloween-promotion-usa/
Source: http://funpicc.blogspot.com/2012/01/coca-cola-zero-pepsi-1-well-played.html

Too Big To Fail: Coca Cola generates majority of its revenues from selling the concentrate for soft drinks. The formula for this concentrate has been one of the most well-kept trade secrets and it is this taste that people buy. The latest production technologies have been adopted to help the company decrease its costs exponentially. Coca Cola has been both aggressive and creative with its marketing strategies. From hiring famous people, to catchy taglines and tie ups with restaurant chains, has helped them earn extraordinary rents. Although the company has protected its secrets, the tastes have been reverse engineered to be replicated by other firms. Even then, the consumers still stick to Coca Cola because of the brand factor that has been built over the years.

Coca Cola has faced a lot of heat, having been subject to a number of lawsuits and battling the food regulations of the individual countries. Speculations of Coca Cola being injurious to health has led to their products being under investigation. [4] Such sentiment among consumers can decrease the demand for their products. To tackle this problem, Coca Cola is diversifying its product base by introducing healthier variants e.g. Coke Zero, Diet Coke. Various geographical locations have different tax structures or other government regulations which can lead to different costs of production. Since the company does not enjoy an excessive pricing power, it can lead to reduced operating income in particular regions (E.g. Soda tax recently introduced in Philadelphia).[5]

The graph shown below depicts the performance of 'KO US Equity' stock over the past 20 years. We can see a prominent dip in the price of stock during the recession period but there has been an upward trend in the price since then.



Source: http://www.amigobulls.com/

The soda sales have been consistently decreasing in last 11 years. However, the price of the stock hasn't dropped proportionately, mainly because of 2 factors:

- Improvements in production process has led to reduced costs, thereby increasing operating profits.
- Consistent buy back of shares by the company, helping to keep the EPS up.

To handle the impact of decreasing sales, new bottling technologies have been implemented since June to improve their operating income. Coca Cola's future plans include refranchising their company structure to improve its efficiency, and to reset businesses in countries where revenues have considerably dropped.[6] Such measures taken by the company are short term ventures as they do not promise stability in future. Even the recent M&As have been within the beverage industry, which hasn't really diversified their market. On the other hand, their archrival Pepsi has stakes in the food industry to diversify their product base. This has led Pepsi to have increased revenues over the years and leaving Coca Cola with decreased revenues.

In summary, Coca Cola owns one of the most marketable brands. With decreasing demand for soda in the world, it should consider diversifying its product base by entering into other market segments such as, intra-department (e.g. still beverages) or inter-department (e.g. food). Failing to do so might hurt the business of the company in the long run.

References:

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