

## PepsiCo Inc.

## BFY Brands: Healthy “Pop”portunity

**Stock Rating/Industry View:** Equal Weight/Neutral**Price Target:** USD 135.00**Price (02-Dec-2019):** USD 135.88**Potential Upside/Downside:** -1%**Tickers:** PEP

Good evening,

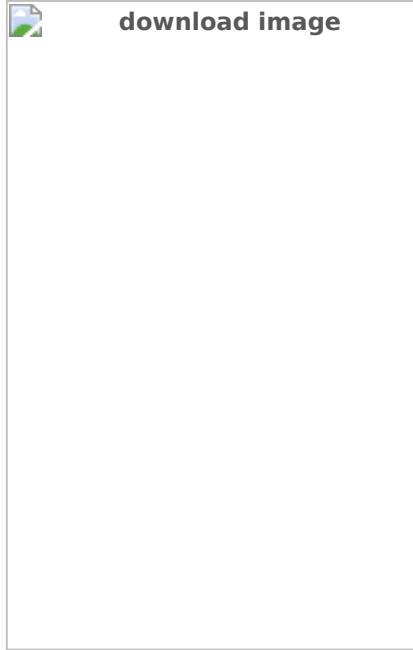
Earlier this evening, PepsiCo announced a definitive agreement to acquire BFY Brands, the parent company of high-growth, better-for-you snacking brand PopCorners. While we don't expect the deal to be financially material to 2020 earnings, we believe it has interesting strategic implications for PepsiCo's broader snacking mandate.

**We view the PopCorners acquisition as yet another example of PepsiCo's efforts to future-proof its Frito-Lay snacking portfolio...**With consumers increasingly embracing “health and wellness” trends, PepsiCo has taken on a number of initiatives over time to align its snacking portfolio with a growing demand for better-for-you products. This has included: 1) improving the nutritional profile of its core brand portfolio by the reducing its saturated fat and sodium content; 2) launching healthier line extensions under existing brand equity umbrellas eg. “Simply” and “Baked!” Tostitos, Lay's, Cheetos & Ruffles, and Smart50; and 3) bolt-on M&A (2005: Stacy's Pita Chips; 2018: Bare Snacks). The acquisition of BFY Brands is consistent with this strategy, allowing PEP to expand into the popped chips sub-category with a product line-up including the flagship PopCorners brand as well as brand extensions such as Flex Protein Crisps and Flourish Veggie Crisps (both launched this year). Notably, the calorie profile of the portfolio PepsiCo would acquire underindexes both competitor brands on shelf (eg. popchips) as well as the bulk of PEP's existing better-for-you portfolio (Figure 1).

**...with ample opportunity for Frito-Lay to sustain or even accelerate revenue growth for the brand by leveraging its robust DSD footprint to expand distribution.** As a small but fast-growth brand, there is plenty to play for in terms of incremental distribution opportunity for PopCorners by simply plugging it into PepsiCo's extensive direct-store-distribution network. Additionally, we would note that a comparison of the brand's retail footprint versus other better-for-you brands, like Smartfood for example, would indicate significant opportunity to capitalize on distribution opportunities in the convenience and mass channels in particular. Specifically, while PopCorners' retail exposure skews strongly toward the Food channel (~76% of sales), SmartFood is more evenly split between Food, Mass and Convenience (Figure 2).

**Financial Terms:** As per scanner data, BFY Brands has an LTM revenue base of \$53mm and grew +55% over this period. Assuming the company is able to sustain these levels of growth under PepsiCo's ownership and that its EBIT margins track in line with the broader Frito-Lay business, we would expect the deal to be 1c accretive to earnings in 2020 and neutral in 2021. Our math assumes a 30:70 debt-to-cash financing split and a 4.5x LTM EV/Sales multiple (using Hershey's acquisition of Pirate's Booty in 2018 as a corollary), implying an LTM EV/EBITDA multiple of 13x and a purchase price of ~\$240mm.

**Figure 1: PopCorners' calorie profile underindexes both competitor brands on shelf (eg. popchips) as well as the bulk of PEP's existing better-for-you portfolio.**



Source: Barclays Research

\*Owned by VMG Partners

***Figure 2: A comparison of the brand's retail footprint versus Smartfood would indicate significant opportunity to capitalize on distribution opportunities in the convenience and mass channels.***



Source: Barclays Research; U.S Nielsen

As always, please feel free to call with any questions or comments.

Best,

Lauren

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**Mentioned Stocks (Ticker, Date, Price)**

**PepsiCo Inc.** (PEP, 02-Dec-2019, USD 135.88), Equal Weight/Neutral, A/CD/CE/D/J/K/L/M

**Valuation Methodology:** Our \$135 price target is based on a 23x P/E multiple on CY20 EPS of \$5.88.

**Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target:** Upside: 1) Emerging markets (particularly Russia) accelerate, 2) New innovation helps PEP exceed revenue expectations, 3) PEP benefits from domestic tax and fiscal policy changes. Downside: 1) Increases in commodity and fuel prices offer less margin upside, 2) Continued pressure on North America Beverages business, 3) Slowing trends in core Frito business.

### Ratings and Price Target History:

PepsiCo Inc.

Currency=USD



Source: IDC, Barclays Research

Publication Date	Closing Price	Rating	Adjusted Price Target
04-Oct-2019	140.28		135.00
10-Jul-2019	134.41		125.00
18-Apr-2019	127.09		119.00
15-Feb-2019	115.91		111.00
07-Jan-2019	109.53		104.00
03-Oct-2018	107.52		109.00
11-Jul-2018	112.54		111.00
27-Apr-2018	101.71		108.00
15-Mar-2018	111.99		113.00
14-Feb-2018	109.11		116.00
05-Oct-2017	110.45		113.00
12-Jul-2017	114.77		114.00
27-Apr-2017	112.64		113.00
17-Feb-2017	108.15		111.00
16-Feb-2017	108.12		104.00
09-Jan-2017	103.46	Equal Weight	102.00

Source: Bloomberg, Barclays Research

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