

# PepsiCo: 12- Chapter SVA Teardown

# 1. Executive Summary & The SVA Mandate

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PepsiCo (PEP) presents as a mature, wide-moat consumer staples enterprise generating substantial and consistent Economic Profit. The current ROIC of  $\sim 13.0\%$  stands significantly above a WACC of  $\sim 6.9\%$ , creating a value spread of  $+6.1\%$ . This is the hallmark of a disciplined, well-managed operation.

However, the market valuation of  $\sim \$233\text{B}$  implies a forward growth expectation that is non-trivial for an enterprise of this scale. Our Reverse DCF analysis indicates the market has priced in a  $4.5\%$  NOPLAT growth rate over the next five years. Achieving this is the central challenge.

The primary strategic tension is the conglomerate structure. While the "Power of One" synergy between snacks (Frito-Lay) and beverages is the stated strategy, the superior margin and ROIC profile of the snacks division presents a clear vulnerability to activist intervention aimed at unlocking value via a spin-off.

Our mandate is to deconstruct the mathematical drivers of value and identify the operational levers required to meet, and exceed, the market's baked-in expectations. Margin defense against inflation and disciplined capital allocation away from low-return segments are paramount.

## 2. The Value Creation Moat (Qualitative Analysis)

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### 1. Core Moat Components:

**Intangible Assets (Brand Portfolio):** A multi-billion-dollar portfolio of 23+ brands including Pepsi, Lay's, Doritos, Gatorade, and Quaker. This brand equity creates pricing power and a durable consumer connection.

**Scale-Based Cost Advantages:** Unparalleled global manufacturing and distribution footprint drives significant economies of scale in procurement, production, and logistics. This creates a formidable barrier to entry.

**Distribution Network:** A deeply entrenched direct-store-delivery (DSD) system for the snacks division provides a significant competitive advantage in securing optimal shelf space and maintaining product freshness, a moat that is difficult and capital-intensive for competitors to replicate.

### 2. M&A Vulnerabilities & Structural Risks:

### 3. Methodological Financial Diagnosis

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This is the raw calculus of value creation. All figures are based on Trailing Twelve Months (TTM) and standard SVA adjustments.

Metric	Calculation	Value	Diagnosis
NOPLAT	$EBIT * (1 - \text{Effective Tax Rate})$	\$10.0 B	The core operating cash earnings of the enterprise.
Invested Capital	$\text{Net Working Capital} + \text{Net PP\&E} + \text{Other Assets}$	\$77.0 B	The total capital deployed to generate NOPLAT.

## 4. The ROIC Tree De-composition (L&T Framework)

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ROIC is a function of profitability (NOPLAT Margin) and asset efficiency (Capital Turnover). We deconstruct it to identify the primary value driver.

NOPLAT Margin x Capital Turnover

(10.9%) (1.19x)

(NOPLAT / Sales) (Sales / Invested Capital)

\$10.0B / \$91.8B \$91.8B / \$77.0B

## 5. Analyst Consensus vs. SVA Reality

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Analyst Consensus (The Street View): Focuses on quarterly EPS beats, forward P/E multiples, and dividend yield. Views PEP as a stable, "defensive" income stock. The narrative is driven by price-to-earnings expansion and incremental revenue growth. This approach masks the underlying capital efficiency and the magnitude of cash flow required to sustain the current valuation.

SVA Reality (Intrinsic Value): The current share price is not a reflection of past earnings; it is the discounted value of \*future\* cash flows (Economic Profit). The SVA reality is that PEP must generate ~\$4.7B in Economic Profit \*annually\* and grow that profit at ~4.5% just to meet the expectations already priced into the stock. Any deceleration leads to mathematical value destruction via multiple compression, regardless of EPS performance.

## 6. The Spread-Growth Matrix

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This matrix plots the ROIC-WACC spread against NOPLAT growth, defining the nature of shareholder value creation.

Current Position: PEP is firmly in the "Premium Value Creator" quadrant (High Spread, Moderate Growth).

Economic Profit Sensitivity Analysis:

| NOPLAT Growth -> | 2.0% (Stagnation) | 4.5% (Market Expectation) | 6.0% (High Performance) |

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## 7. Expectations Investing (Reverse DCF)

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We reverse-engineer the current Enterprise Value (EV) of ~\$273B to find the implied NOPLAT growth rate the market expects.

Current Enterprise Value (EV): \$273B

Current NOPLAT: \$10.0B

WACC: 6.9%

Terminal Growth Rate (g): 2.5% (assumed long-term inflation)

## 8. Corporate Structure & M&A Vulnerabilities

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Segment De-composition (Approx. Contribution to EBIT):

1. Frito-Lay North America (FLNA): ~45%. The crown jewel. High margin, high ROIC, strong growth.
2. PepsiCo Beverages North America (PBNA): ~25%. Lower margin, intense competition, high capital requirements.
3. International (Europe, LatAm, AMESA): ~25%. Mix of developed and emerging markets. Key growth engine, but with FX and geopolitical risk.
4. Quaker Foods North America (QFNA): ~5%. Low growth, lowest margin. A clear portfolio laggard.

## 9. TSR (Total Shareholder Return) Decomposition

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We deconstruct the required return to illustrate the components shareholders are paid from. Assuming a target TSR of 9.0% (a typical expectation for a blue-chip).

TSR = Dividend Yield + NOPLAT Growth + Change in Multiple

Component	Calculation	Value	Implication
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Dividend Yield shareholders.	Annual Dividend / Share Price	3.2%	The baseline cash return to

## 10. Macro-Economic Positioning & Risk Assessment

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### Positioning (Strengths):

Defensive Demand: Consumer staples nature provides resilience during economic downturns.

Pricing Power: Strong brand equity allows PEP to pass through inflationary input costs to the consumer, defending NOPLAT margin.

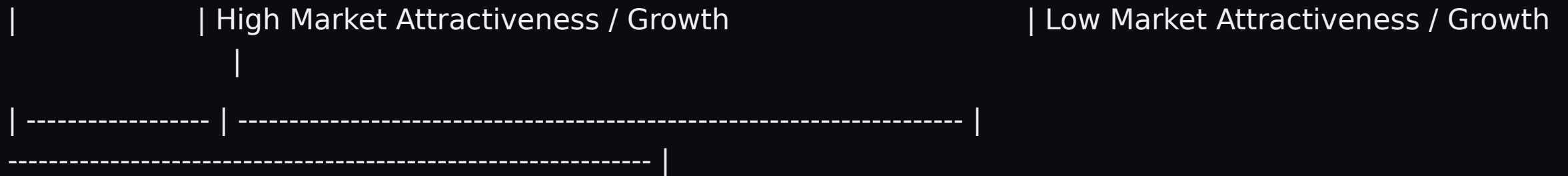
Geographic Diversification: Global footprint mitigates risk from any single market's downturn.

### Risk Assessment (Weaknesses):

# 11. MBB Matrix Analysis (Portfolio Health)

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We plot PEP's business units on a standard GE-McKinsey / BCG matrix to visualize portfolio health and capital allocation priorities.



STARS: <br> - Energy Drinks (Rockstar) <br> - "Healthy" Snacks (Bare, Off The Eaten Path) <br> - Emerging Markets (India, Vietnam) | CASH COWS: <br> - Frito-Lay North America <br> - PepsiCo Beverages North America |

QUESTION MARKS: <br> - Plant-based ventures <br> - Direct-to-Consumer (D2C) platforms | DOGS: <br> - Quaker Foods North America |

## 12. The Final Mandate (Strategic Recommendations)

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Based on the preceding SVA, the following actions are mandated to maximize long-term shareholder value:

1. **Execute Portfolio Purity:** Initiate an immediate strategic review of the Quaker Foods North America (QFNA) division. The objective is divestiture. The capital and management focus trapped in this low-return Dog must be redeployed to higher-growth, higher-return segments. This single action will provide a material uplift to aggregate ROIC.
2. **Optimize Capital Allocation:** Implement a more rigorous, ROIC-based capital budgeting process. Shift discretionary capex and A&M spending from the mature PBNA cash cow towards the FLNA and International Stars. All projects must have a positive projected Economic Profit delta.
3. **Defend the NOPLAT Margin:** Launch a corporate-wide operational efficiency program ("Margin Shield") targeting a 50 basis point reduction in COGS/SG&A as a percentage of sales. This is a non-negotiable defense against inflationary pressures and is more value-accretive than chasing low-quality revenue growth.
4. **Pre-empt Activism:** Proactively communicate the SVA case for the "Power of One" strategy. Quantify the cost and revenue synergies between the beverage and snacks distribution networks. If these synergies are less than the potential value-unlock from a spin-off, the board must reconsider the corporate structure. Simultaneously, accelerate cash return to shareholders via share buybacks to increase EPS and signal