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Case study on Coca-Cola Diversification Strategy, 2018

COCA-COLA'S FUTURE GROWTH STRATEGY: DIVERSIFICATION?

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COCA-COLA'S FUTURE GROWTH STRATEGY: DIVERSIFICATION?

The year 1886 was the birth year of the world renowned, mega-cap company Coca-Cola Co. It all began when a pharmacist named John Pemberton was experimenting with carbonated beverages and created a medicinal drink to sell to drug storesⁱ. The first ever Coca Cola was made with cocaine and wine, but later the cocaine was substituted out with the Kola nut to bypass the alcohol restriction in 1885. Due to the use of the Kola Nut in the syrup mixture, Frank M Robinson, the first Marketer of Coca Cola coined the name Coca Colaⁱⁱ, which quickly started to gain popularity. In fact the word Coca-Cola is the second most used and understood word after the word "Okay" worldwideⁱⁱⁱ. In order for Coca Cola to reach this point of growth, it has a long and enduring history of strategic partnerships, alliances and acquisitions.

Company Background

In 1894, the company was sold to Asa Candler for \$2,500 and since then the company has seen various management shifts and has ventured all over the world. Coca Cola has a long and successful history of acquiring various food and beverage companies from Minute Maid in 1960 to Odwalla in 2001^{iv}, along with entertainment companies such as Sony in 1989^v and Columbia Pictures in 1982^{vi}. Now, Coca Cola Co. has ventured into the apparel and accessories business, with the partnership of Kith to launch a licensed KithxCoca-Cola line in 2018^{vii}. Even though Coca-Cola has diversified its operations, yet their flagship product is still the biggest revenue earner. They have been, and are currently, expanding into the flavored drink lines, which can take the spotlight away from their star, the original Coca-Cola drink. Is moving into other product markets a good strategic move for Coca-Cola Co.?

Carbonated Soft Drink(CSD) Industry

The Carbonated Soft Drink (CSD) industry generated \$212.1 billion in revenue in 2018 (see appendix A)^{viii}, which includes two of the biggest players, Coca-Cola Co. and PepsiCo. The CSD market is a maturing industry with little room to grow due to the changing economic, health, and environmental factors. In addition, due to the nature of the diversification of the CSD companies' products and services, CSD companies are experiencing growth in some areas such as healthy drink offering, and stagnation in flagship products such as the original Coca-Cola, while some parts of the company have reached maturity such as sugary fruit juices from concentrates. As a result, companies are applying different strategies to each of their departments and product segments. One of the biggest CSD's operations is the sale of carbonated sodas, and over the past five years, CSD companies have struggled to bring in profits from the sales of their flagship products. The flagship products of CSD companies are also becoming less attractive to consumers due to various issues such as high level of sugar in Coca-Cola's original drink, along with the increased cost of production.

Due to the decreasing demand of the traditional drinks and changing consumer taste preferences, the industry's annual revenue is decreasing at an annual rate of 3.0%^{ix} in developed countries and regions, such as the U.S and Europe. In the emerging markets, or developing countries, the popularity of sugary, carbonated drinks is constantly growing and increasing. This is why CSD companies like Coca-Cola Co. and PepsiCo. are primarily focusing on promoting their flagship products to the developing markets instead of introducing and promoting innovative drinks in emerging markets. The global promotion and global sale of companies' original, flagship product are helping in balancing the decreasing revenue from the western, more developed countries. Even with the increasing percentage of the US. discretionary income, the demand for sugary, carbonated drinks is gradually decreasing in the US. due to the raise of a health conscious society.

CSD Industry Competitive landscape

Competition in the CSD industry has been very intense among a few big players such as PepsiCo., Dr. Pepper Snapple Group, Cott, and National Beverage Company. In 2018, Coca-Cola held the largest market share at 42.8% while PepsiCo. held 25.6 %, Dr. Pepper holds 17.9%, Cott held 3.7% and finally, the National Beverage company held 2.9% along with other local brands that held 7.1% of the CSD Industry market share (See Appendix B, Exhibit 1). Over the past five years, Coca-Cola has seen a decline in their market share. This could be the result of a higher level of diversification at companies like PepsiCo. or Dr. Pepper Snapple group, who have a wide range of partnership and offer products beyond the carbonated realm, which can help capture a larger share of the CSD market. The reason PepsiCo has a higher potential of capturing the market share is that it diversifies its product offering via strategic partnerships and acquisitions. PepsiCo recently acquired SodaStream in August 2018, along with Bare Foods in May 2018, KeVita in November 2016, Mabel in November 2011, Health Warrior in October 2018, and Doritos, along with many other food and beverage acquisitions. PepsiCo's outgoing CEO put a lot of emphases in getting in the healthy beverage market to keep increasing their market share and their profits.

PepsiCo's outgoing Chief Executive Indra Nooyi, more than a decade ago staked her career a plan to expand the company's portfolio into healthier, more nutritious products. More recently, the soda-and-snacks giant has been under pressure to restructure its U.S. beverage business after it shifted too much marketing money and shelf space to newly launched brands in hybrid categories such as Izze Fusions, a combination of fruit juice and soda.^x

PepsiCo's is venturing to realms other than its original product of Pepsi-Cola. Additionally, The National Beverage Company has a mix of Food and Beverage acquisitions, such as Faygo, LaCROIX and Shasta Food Services. Dr. Pepper, on the other hand, does not have many Food/Snack related acquisitions; it only has beverage related acquisitions such as Core Nutrition, Seven-Up Bottling Company, and Keurig along with few other beverage companies. (see Appendix B, Exhibit 2). Similarly, Coca-Cola Co. has mostly beverage related acquisitions, such as Minute Maid, Vitamin water, Powerade, and Zico just to name a few (See Appendix B, Exhibit 3). Nowadays, in order to stay ahead of the competition, companies need to venture beyond their flagship products in order to stay profitable.

Industry Challenges

One of the biggest issues affecting the industry is the shift towards a health-conscious society, owing to “the growing health concerns, consumers in North America and Europe have curbed their intake of sugary beverages such as carbonated soft drinks, fruit juices, and traditional sports drinks^{xi}”. Most beverages offered by CSD companies are clinically considered very unhealthy and the consumption of the sugary carbonated beverage is linked to most health problems. Therefore, people are steering away from them due to the increased prices of health care insurance, policies, and healthcare bills. This is not only linked to the high rate of child obesity in the US. but CSD products are also a high concern in Latin and Central America, where the carbonated beverage is consumed regularly and even on a daily basis. The Latin American countries are now facing an obesity epidemic, which can lead to life-threatening problems. In addition to health consciousness, the average American is becoming a lot more aware of their environmental footprint. As a result, they are refusing to purchase products that are bottled using non-biodegradable plastic. This is not just an American problem, but a global epidemic. Coca-Cola has been “long criticized by environmental advocates for producing billions of plastic bottles that end up in landfills and oceans^{xii}.” Another trend that is affecting the industry is the consumer’s changing taste preferences; consumers are looking for more functional drinks, and drinks that provide a wide variety of different and non-traditional flavors.

Industry opportunities

Due to the shift towards health consciousness of Americans and other developed countries, the changing trends, consumer lifestyles, and preferences, can all present some opportunities for CSD companies to capitalize on. The CSD industry is seeing changes in the companies who are slowly expanding into completely new and different markets in search for growth opportunities. Some may argue this is blurring the line between their original product offerings and the company as a whole, since their value proposition, mission, and vision are built around their flagship product such as the original Cola. Currently, diversifying has become a main source of survival for the mature soda companies. The changing consumer behavior is moving towards a lifestyle that is based on mixing traditional drinks with new ingredients or flavors and creating a

new drink, that may act as functional drink, a leisure drink or hybrid of functionality and taste, right at home. This provides the CSD companies with an opportunity to get into a different market, that a consumer like Lisa Fink is in.

Shifts in the beverage aisle are being driven by people like Lisa Fink, who used to drink black coffee in the morning and again in the afternoon. Now, the 46-year-old personal trainer in Thousand Oaks, Calif., drinks chai tea with bone broth, protein powder and coconut creamer—a drink that serves as breakfast—and switches to tea and sparkling water for the rest of the day. Sometimes, as a treat, she has a can of Zevia cola made with stevia, a zero-calorie, plant-based sweetener.^{xiii}

A societal shift towards healthy-living and product functionality is becoming the norm and the companies who can not keep up with the changing trends are seeing a high rate of diminishing returns. In order for CSD companies to stay competitive they need to venture into realm other than carbonated sodas. Nowadays, “no longer do soda companies, coffee companies and alcohol companies stay in their lanes”^{xiv} which is seen as a new and increasing trend among sugary beverage companies. But figuring out the ever-changing consumer preferences is pretty difficult and tricky, and “the answer, for many companies, has been to mix their traditional beverages with popular new ingredients to create hybrids.”^{xv} Which seems like a viable solution but “all the new varieties have created confusion for retailers and the shoppers who traverse the supermarket trying to find their favorite drinks.^{xvi}”

Coca-Cola’s Resource and Capabilities

Coca-Cola’s resources and capabilities set it apart from its competitors. Coca-Cola had a net operating revenue of \$35.4 billion, which they can reinvest in various new markets and projects in order to grow. They have up-to-date technological resources, which helps speed up the production process. Human capital is another important resource Coca-Cola prides themselves on. The employee engagement and employee motivation drive the growth of the overall company. Capabilities are another source of competitive advantage. Their marketing capabilities strengthen the brand image and increases consumer awareness which can achieve long-term growth. Brand awareness is one of their largest intangible asset, since Coca-Cola has penetrated into 200^{xvii} plus countries’ Markets. Commercial leadership capability provides their customers

with various solutions for their customers to grow. Franchise leadership capability helps the company and the bottling partners to achieve an increased level of growth rate.

Current State of Coca-Cola Co.

Coca-Cola Co. holds more than half (60%)^{xviii} of the market share globally and 42.8% in the U.S. As of 2018, Coca-Cola Co. holds the title for the most valuable soft drink company in the world with \$68 billion as their brand value. But over the past four to five years the brand value has been decreasing; it went from being \$83.84 billion in 2015, to \$78.14 billion in 2017, and increased just a little in 2018 to \$79.96 billion (see appendix C, exhibit 1). Both Coca-Cola's global revenue and global net operating revenue have experienced decreases over the past five years. Net operating revenue went from \$48.02 billion in 2012, to \$35.41 billion in 2017, which is a 26.25% decrease over the past five years. Similarly, the operating income went from \$10.78 billion in 2012, to \$7.50 billion in 2017, which is a 30.41% decrease over the past five years. The stagnation of revenue and profits is a result of the changing trends that the whole industry is experiencing. The consumer preferences are changing, stricter environmental pressure and regulations are going in to effect, and the competition is innovating their products and practices.

Coca-Cola's Strategy

Coca-Cola is still pursuing a growth strategy even though the CSD is a mature market, as a result, Coca-Cola has to try different avenues to create a wide variety and diversify their product lines, so they can get their foot in different market segments, and ultimately increase their revenue. To grow, Coke has mainly pursued a diversification strategy and the main way Coke has pursued diversification is through acquisitions; Coca-Cola has 11 acquisition, more than any of its competitors. Coca-Cola already has a tendency of acquiring companies out of their usual segment, such as the acquisition of Columbia Picture Entertainment in 1982 and recently Costa Limited in 2018; which is a coffee-based company that operates globally. Now Coca-Cola will have a strong presence in the coffee segment of the market. Additionally, Coca-Cola acquired both Mojo Beverage and Tropicana in September 2018, along with Zico in April 2012, Fuze Beverage in May 2007, Barq's in May 1995 and Minute Maid in December 1960. Coca-Cola Co.

has mainly invested in the juice and water segments of the beverage industry over the past couple of decades, but there are more opportunities for Coca-Cola to further explore.

How can Coca-Cola grow in the future?

Even a multi-billion dollar company cannot stay on top of the list forever unless it has a growth strategy in place. If a company wants to keep competing and surviving in a very competitive landscape, it needs to keep innovating their growth strategy. Coca-Cola is positioned in a mature market segment, where it stays ahead of its competition through utilizing its resources, capabilities and its diversification strategy. As competition increases, should Coca-Cola keep acquiring new and unusual product lines or stay within their flagship product but keep innovating them, or should they start making their own drinks with different and untraditional ingredients and flavors? As Coca-Cola Co. progresses, what growth strategy should it pursue? Based on industry trends, what opportunities can be capitalized on for continuous growth? With current resources and capabilities, how can Coca-Cola grow in the future? Is diversification the best strategy for future growth? These are few of the questions that come up when a mature company is trying to stabilize or grow in the future.

Appendix A

CSD Industry Revenue Growth

Revenue Growth

Year	Revenue \$ million	Growth %
2003	175,909.5	0.0
2004	194,005.2	10.3
2005	211,488.8	9.0
2006	210,184.1	-0.6
2007	230,687.3	9.8
2008	244,131.9	5.8
2009	226,980.6	-7.0
2010	233,027.7	2.7
2011	253,092.5	8.6
2012	251,888.9	-0.5
2013	247,194.2	-1.9
2014	245,523.0	-0.7
2015	223,462.5	-9.0
2016	209,576.2	-6.2
2017	211,087.7	0.7
2018	212,068.2	0.5

Appendix B : CSD industry competitive landscape

Exhibit 1: Market share of CSD companies in the U.S.^{xix}

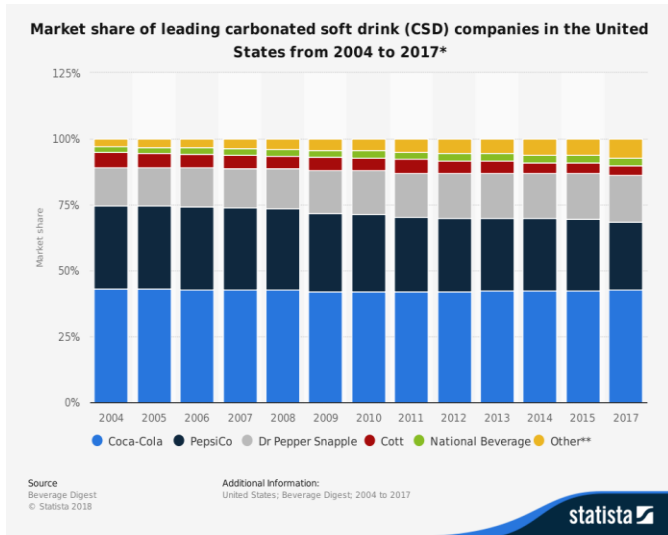


Exhibit 3: Coca-Cola's acquisition.

				
Market Share (%)	25.6%	14.5%	2.9%	42.8%
Annual Revenue	\$64 Billion	\$6.6 Billion	\$1.0 Billion	\$ 33.9 Billion
Advertising spending	2.4 Billion	4.8 Million	\$136,000(in 2013)	\$899 million
Acquisitions and Partnerships	<ul style="list-style-type: none"> • KeVita • Doritos • Health Warrior • SodaStream • Bare Foods • Frito lays 	<ul style="list-style-type: none"> • Core Nutrition • Davis Beverage Group • Seven Up bottling company • Keurig 	<ul style="list-style-type: none"> • Faygo • LaCROIX • Shasta Food Services 	<ul style="list-style-type: none"> • Powerade • Minute Maid • Golden Peak • Vitamin water • Zico

Exhibit 2: CSD industry's competitive landscape

Appendix C: Coca-Cola Co.'s Brand Value and Global Revenue

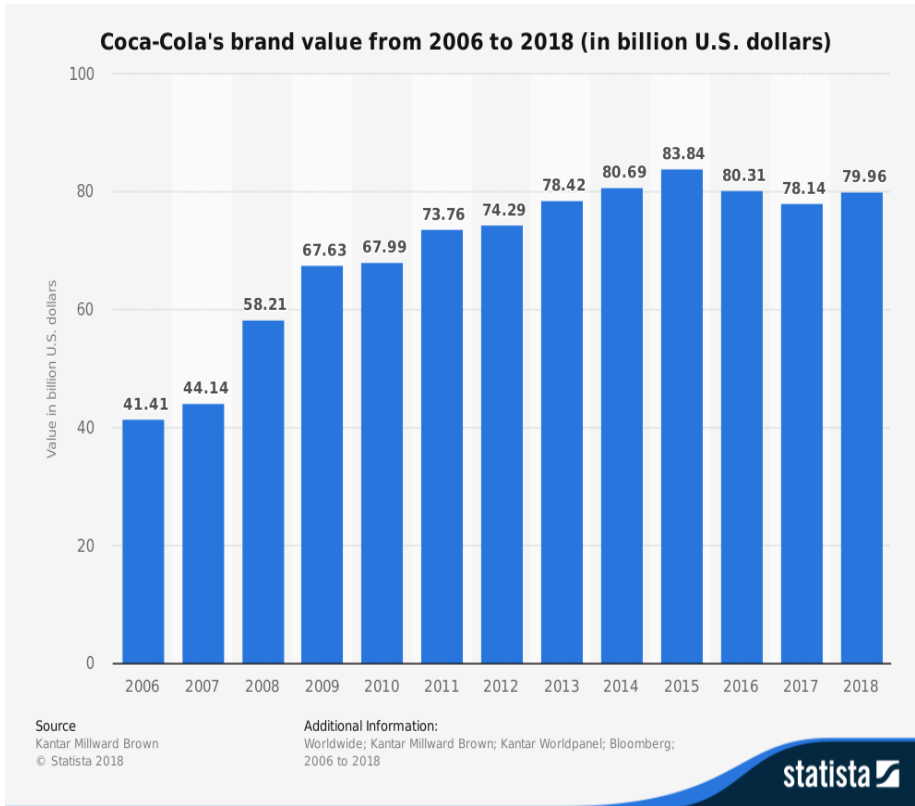


Exhibit 1: Brand value of Coca-Cola Co. from 2006 to 2018.

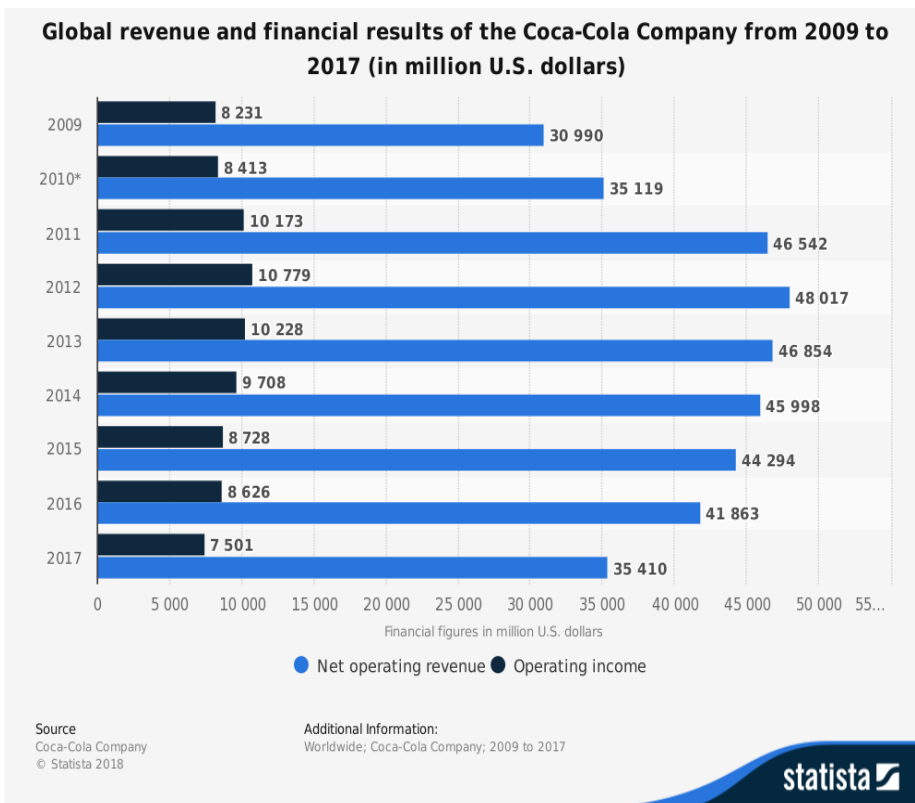


Exhibit 2: Coca-Cola Co.'s total global revenue from 2009 to 2017.

Endnotes

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- ^{xvii} “Who We Are.” *The Coca-Cola Company*, 2018, www.coca-colacompany.com/careers/who-we-are-infographic.
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