

Coca-Cola (NYSE: KO) Company Valuation Project

Company Profile Intro:

The Coca-Cola Company has come a long way since the first \$50 it made its first year to the international scale business, we all know now. Unlike the secret ingredient of cocaine that was included in the beverage in the early life of The Coca-Cola Company, the addiction for enjoying the non-alcoholic beverage has not subsided. The Coca-Cola Company is an American beverage company incorporated in 1892. John Pemberton, a pharmacist based in Atlanta, Georgia invented the first Coca-Cola mix syrup in 1886. The product, a mix of liquid caramel and carbonated water, has set the way for Coca-Cola to be sold in over 200 countries.

Since its inception, the Coca-Cola company has grown to the number one nonalcoholic beverage company in the world with more than 3,500 beverages and 500 brands in its product portfolio. Coca Cola Company operates around the world in North America, Africa, Asia and the Middle East and more than 200 countries. In the beverage & ice manufacturing industry, the Coca-Cola company emphasizes safe consumables that are approved by the USDA which attracts potential customers and investors. The firm is headquartered in Atlanta, GA, and has over 200 bottling partners worldwide, employing more than 700,000 people. “Coca-Cola has been consistently ranked as the top soft drink brand worldwide, with a global brand value of over 71 billion U.S. dollars. Other soft drink brands manufactured and sold by the Coca-Cola Company include Diet Coke, Sprite, and Fanta.” It also owns the largest market share and has a market capitalization of 102 billion in US dollars and the industry average is 75 billion in USdollars.

Coca-Cola Projects:

The next decade will be very exciting for the Coca-Cola Company. The company is expecting to make multiple strides in different areas such as sustainable packaging, product development, and acquisition opportunities. The Coca-Cola Company has outlined a strategic process to reorganize and better optimize the Coca-Cola system for drinks that are positioned to capture growth in a fast-changing marketplace. The innovations in packaging design, increase in bottle collection rates, and investments in renewable energy for manufacturing are the different ways that Coca-cola is moving towards the future.

Sustainable packaging: Coca-Cola has pushed forward a World Without Waste initiative focused around making 100% of the packaging recyclable globally by 2025; using at least 50% recycled material in

the packaging by 2030; collecting and recycling a bottle or can for each one they sell by 2030; and by 2030, they aim to have at least 25% of beverages worldwide by volume sold in refillable/returnable glass or plastic bottles or in fountain dispensers with reusable packaging. Also, Coca-Cola unveiled the first-ever prototype bottle made from 100% plant-based plastic that will revolutionize consumer packaged goods.

New Product Development: Coca-Cola has been shifting its efforts from sugary beverages to less sugary alternatives. This initiative has been pushed as soda consumption falls to a 30-year low rate. The company has done an excellent job repositioning its brand by including different options such as energy drinks, coffee, water, sparkling beverages, Diet Coca-Cola, and Coca-Cola zero sugar.

Acquisition Opportunities: In recent years, Coca-Cola has moved into faster-growing areas by acquiring Topo Chico premium sparkling mineral water; spending \$5.1 billion to purchase Costa Coffee; acquiring the remaining stake in Fairlife milk and the drink BodyArmor to compete with Pepsi's Gatorade. Coca-Cola is leveraging its position in the market by diversifying its brand association by acquiring companies that broaden their market reach.

Macroeconomic conditions:

In the light of recovery from Covid-19 in 2020 and 2021, everything looked brighter for the global economy. The war in Europe also causes problems in the global economy as the market faces high inflation. Most banks have already forewarned about the possibility of a recession due to the rising oil and commodity prices, inflation, increasing demand and lacking supply. The majority of banks and economists, however, assume that the temporary conditions will not affect the strong position of the stock market.

Our upside scenario will include the market as it is, strong and unfazed. The downside scenario will include the mild recession that analysts estimate. The average of past recessions estimate a 30% drop in S&P 500, but since this scenario includes a mild recession and the decrease average is highly skewed due to big losses in 2008, we will take 20% instead. Furthermore, KO is less volatile than the market (beta of 0.66) and the company's longevity and diversified brand portfolio (newly acquired businesses, new products) will easily limit the decrease to 8-10%. Lastly, the economic cycle historically estimates that consumer staples tend to do well with increasing inflation and interest rates as outlined in the picture below (See Image A). With everything being accounted for above, we will assume a 6%-8% decrease in the ratio margins rather than 8%-10%.

Beverage Industry report:

The beverage industry, specifically in the U.S., boasts an incredible valuation of 146 billion dollars with the expectation to continue growing and innovating in the upcoming years. Although COVID has strongly impacted all industries, the beverage industry is expected to continue growing at an aggressive rate. The U.S is estimated to host the largest 5 year estimated revenue growth in sales (\$66 billion) for the beverage industry (See Image B). What's more, the average revenue per consumer is expected to keep increasing even with economic downturns (See Image C). The fact is that with COVID forcing many consumers indoors it didn't stop the industry from thriving. Matter of fact, it led to 79 billion dollars of global revenue generated by e-commerce alone(See Image D).

Having made its name by decades of brand building, Coca-Cola is sure to benefit from aforementioned industry growth; however, the industry is not without its drawbacks. Lower consumption of high fructose corn syrup and sugar and the increase in healthy eating habits will pressure sales. Furthermore, the consumers are demanding more and more variety of flavors especially since the service industry has been closed and people took it upon themselves to try out new flavors while in quarantine. Coca-cola has been responding to these threats via product innovation in flavors and amazing sugar-free options. Overall, the industry's position is as attractive as it can be.

MM Analysis:

In analyzing the valuation of Coca-Cola, we utilized the market multiple approach to understand how well the company's stock has performed compared to its competitor. The market multiple consists of the growth rates associated with sales per share (SPS), cash flow per share (CFPS), and earnings per share (EPS) (see Image E). Coca-Cola had stronger numbers in each of the three areas than its competitors. From 2016-2021, its average SPS was \$5.62, with a base -1.75% growth rate, average CFPS was \$29.78, with an 6.01% base growth rate, and average EPS was \$44.24, with a base 8.21% growth rate. In comparison, Pepsi Co.'s 5-year averages were \$2.51 SPS with a 5.5% growth rate, \$17.54 CFPS with a 5.2% growth rate, and 24.14 EPS with a 4.4% growth rate. Coca-Cola's values for these three multiples display a strong business model overall. Compared to its competitor (Pepsi Co.), sales per outstanding share were preferably higher, however its growth rate was negative. This was due to two individual instances where the revenue of Coca-cola dropped drastically. In 2018, Coca-Cola blamed the decline on revenue related to refranchising

its bottle service and the strong dollar. The increase of the strong dollar has negatively affected companies with international sales and profits. The second instance was the global effect of COVID-19, since then the SPS has grown nearly 8% percent. Moving forward, the CFPS was higher than Pepsi Co. indicating that Coca-Cola has much more financial flexibility than its competitor. Finally, Coca-Cola's EPS shows that it is more profitable than Pepsi Co. Given the EPS, Coca-Cola is much more profitable indicating that investors will pay more for the share as the company will have higher profits relative to its share price. The overall analysis of both Coca-Cola and Pepsi Co., shows that Coca-Cola has the stronger market multiples given its greater cash flow (CFPS) to support its profitability (EPS) while maintaining a higher SPS average relative to its competitor.

Ratio Analysis:

Coca-Cola shows strength in the following ratios: Current Ratio (CR), Quick Ratio (QR), Return on Assets (ROA), and Profit Margin (PM) (See Image F). Coca-Cola's 2020 had a strong CR compared to its competitors (1.32 against 0.98). Following the same trend, Coca-Cola's 2020 QR stood at a high 1.09 relative to the competitor's 2020 QR of .81. Additionally, Coca-Cola had a greater return on assets with a solid 2020 ROA of 8.90%. In comparison, Pepsi Co's 2020 ROA of 8.13%, only generating \$0.08 in net income for each \$1 invested in assets. Finally, Coca-Cola's 2020 PM is 23.53%. Pepsi Co, on the other hand, has a 2020 PM of \$0.11 which is \$0.13 less in income per dollar of sales compared to Coca-Cola. For investors this supports the claim that Coca-Cola is much more equipped to meet with short-term debt and is more liquidable than Pepsi Co.

In analyzing these ratios, it reflects how much more efficient Coca-Cola is in operating its business to generate FCF and incredible profit margins. Although, Coca-Cola's numbers have been relatively lower because of a shift in their efforts to improve their bottling operations. Overall, Coca-Cola is still dominating the market space compared to the industry and its primary competitor, Pepsi Co. Coca-Cola's revenue is expected to increase in the upcoming years because of the improved margins that will be created due to bottling operations. This will cause lower associated costs that will bring up profitability in the long run. Coca-Cola is an excellent business with the potential to provide investors with multi year returns.

Growth Assumptions:

Looking at company prospects and capital expenditures, industry health and the outlying economic conditions, we came up with the following growth assumptions: SPS has a base growth of -1.75% with 8% as an upside case and -10% as a downside, CFPS supports 6% as the base and has the capacity to go down to -2% or go up to 12%, EPS is estimated to be 8.21% as default with the chance to go towards 12% or fall behind at 2%. (see Image G)

Sales will grow in line with estimated industry and revenue per customer growth (\$66 billion dollars and \$1500 dollars respectively) estimations and will be challenged by customer shifts in sugar consumption along with their health preferences. Cash flows will increase with aggressive acquisitions of energy beverage (Costa Coffee) and water (Topo Chico) brands in the same sector. The event of a mild recession and another quarantine has the chance to damage said cash flow (6%-8% decrease in valuation). Lastly, EPS will increase because new sustainable packaging (due to their reusability) will decrease operating costs and the industry growth will feed into more sales. The refranchising of its bottles also continues to generate more revenue per drink sold and improve margins of profitability. The denominating factor here again is the possibility of a recession and consumer outlook on beverages with high sugar content. Although there is going to be some concern about economic cyclicalities, Coca-Cola's organic growth and efficiency positions the company to trump most systemic headwinds. That is why we took a lower percentage to decrease aforementioned margins.

Trading Ranges:

Using the value drivers mentioned above, we can come up with the price ranges of \$56.72 to \$66.87 (see Image G). We took the lowest number in CFPS and the highest in EPS because sales have less weight in relation to others in this company. We arranged the weights as such because Coca-Cola is a matured company and their sales move up in an expected way. On the other hand, their projects and ideas move economies of scale and their cash flows to more desirable levels, ultimately increasing the company's bottom line. Hence, we estimate that their capital expenditures and their projects of sustainability carry more significance in moving the stock price than an increased number of sales.

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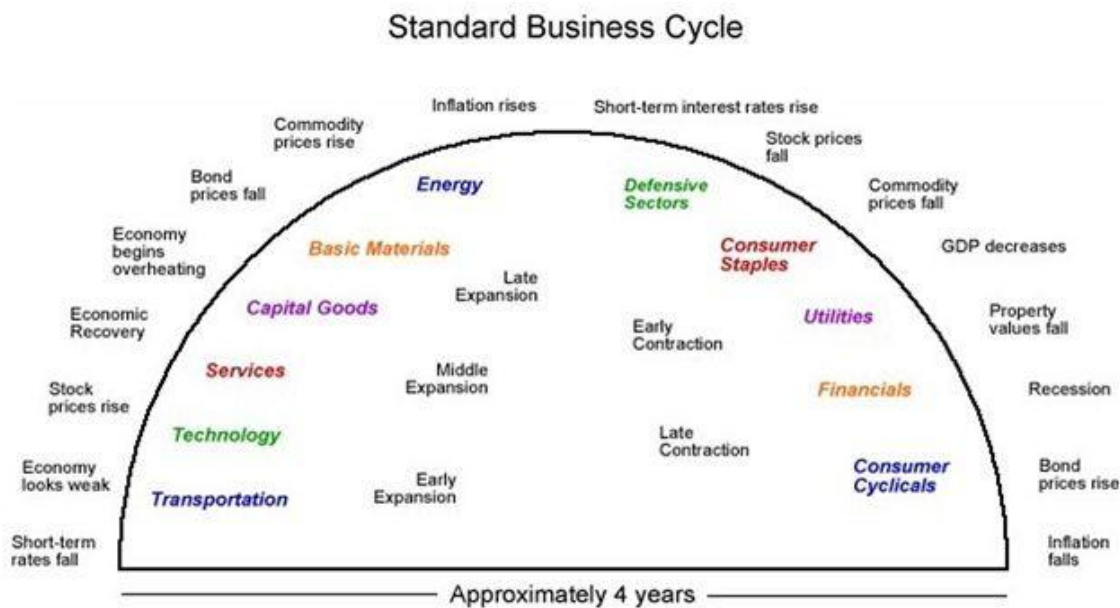
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Image A:



Market Realist

Source: Gerritz Wealth Management

Image B:

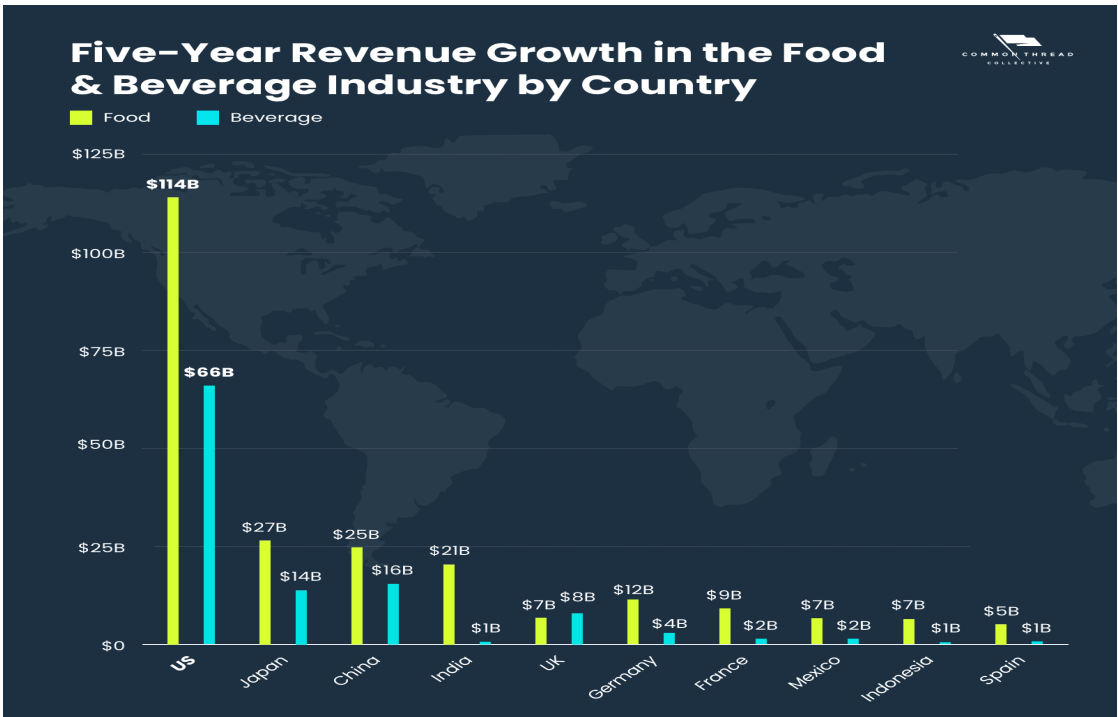


Image C:

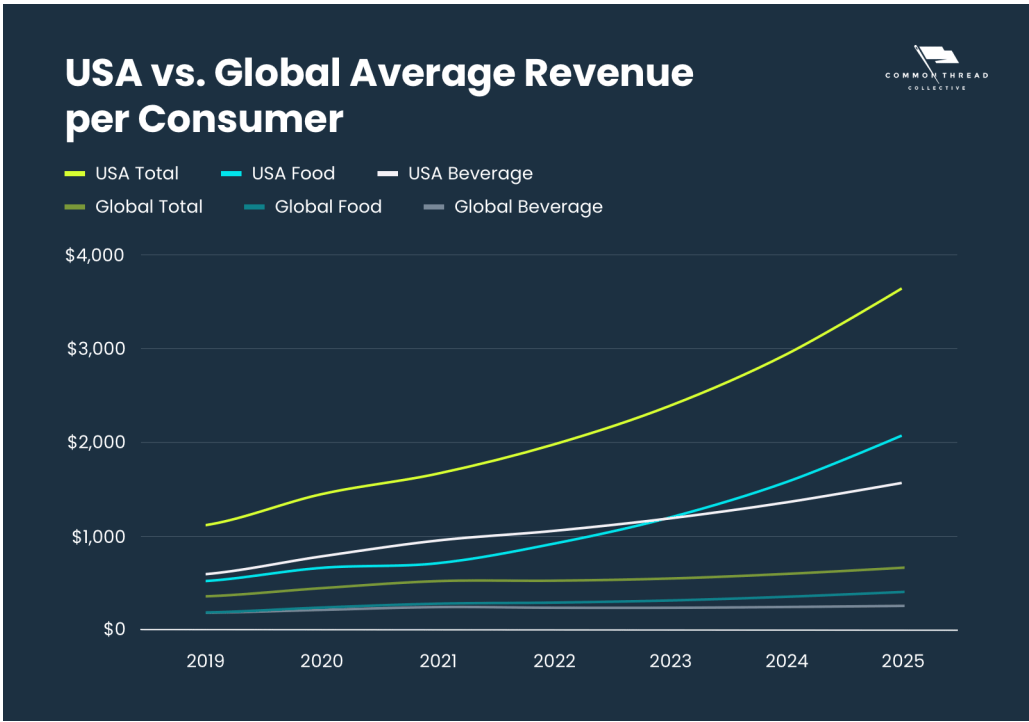


Image D:

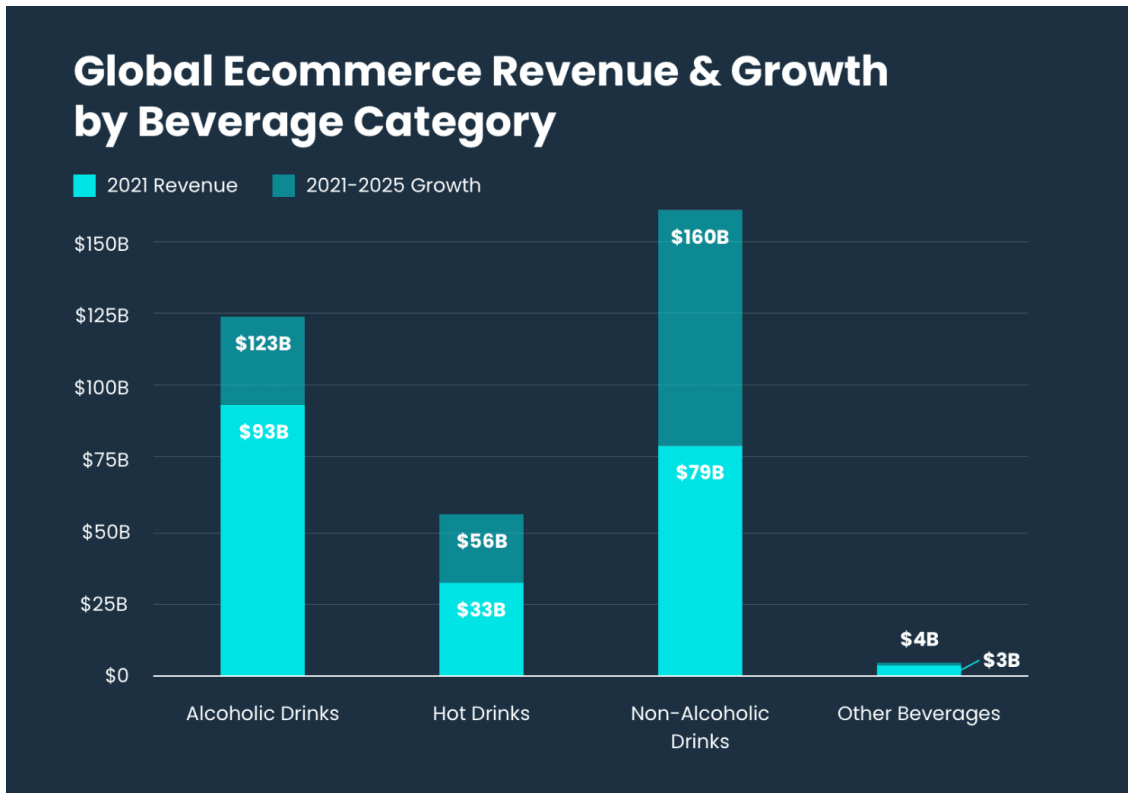


Image E:

		Market Multiple Analysis				
IMAGE E		12/31/2021	12/31/2020	12/31/2019	12/31/2018	12/31/2016
Sales per Share		\$8.94	\$7.67	\$8.71	\$7.46	\$9.76
Price/SPS		6.62	6.93	5.96	5.76	3.61
Cash Flow per Share		\$2.60	\$2.16	\$2.42	\$1.77	\$1.94
Price/CFPS		22.75	24.58	21.45	24.28	18.12
EPS		\$2.27	\$1.81	\$2.10	\$1.52	\$1.53
Price/EPS		26.12	29.44	24.71	28.35	23.06
Closing Prices		\$59.21	\$53.16	\$51.88	\$43.02	\$35.23
Depreciations and Amortization		1,452,000	1,536,000	1,365,000	1,086,000	1,787,000
Shares Outstanding		4,325,000	4,302,000	4,280,000	4,268,000	4,288,000

Image F:

IMAGE F	Pepsi Co.		Coca-Cola
1) Liquidity			
A. Current Ratio	0.98		1.32
B. Quick Ratio	0.81		1.09
2) Asset Management			
Inventory Turnover Ratio	7.62		4.11
days sales in receivables	8.37		34.76
total assets turnover	0.76		0.38
3) Debt Management			
Debt Ratio	3.28		0.78
times Interest Earned	9.04		7.10
4) Profitability			
Profit Margin	10.12%		23.53%
Return on Assets	8.13%		8.90%

Image G:

IMAGE G	Average	Price	Growth	Est Price
	<u>2016-2021</u>	<u>2021</u>	<u>2016-2021</u>	<u>2022</u>
			8% Upside	\$55.76
Sales per Share	5.78	\$51.63	-1.75% Base	\$50.72
			-10% Downside	\$46.47
			12% Upside	\$64.82
Cash Flow Per Share	22.24	\$57.87	6.01% Base	\$61.35
			-2% Downside	\$56.72
			12% Upside	\$66.87
EPS	26.34	\$59.70	8.21% Base	\$64.61
			2% Downside	\$60.90

