Market Talk

Pepsi's New Path to Growth

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PepsiCo is an iconic corporation, widely recognized as Coca-Cola's main competitor in the beverage market. However, its influence extends far beyond carbonated drinks. In fact, nearly half of PepsiCo's U.S. revenue comes from food products, where its dominance in the snack segment is unmatched. The company is the world's largest player in snacks, owning powerhouse brands such as Lay's, Doritos, and Cheetos. In beverages, PepsiCo ranks second globally, just behind Coca-Cola.

Operating in more than 200 countries, PepsiCo generates over $90 billion in annual revenue and is expected to deliver $11billion in profits in 2025. Despite these impressive figures and its leadership in highly competitive markets, PepsiCo's stock appears undervalued compared to its historical performance and industry peers. Currently, the stock trades at a P/E multiple of 18x, well below its historical average of 22x. Relative to the S&P 500 Consumer Staples Index, PepsiCo is also significantly cheaper. For comparison, Coca-Cola trades at a 23x P/E multiple.

In comparison, PepsiCo's stock weakness reflects challenges in its core business. In the North American beverage market, Pepsi has consistently lost market share over recent years, while growth in its food segment has slowed. This underperformance in North America—where the company generates roughly 60% of its revenue—has weighed heavily on overall results, despite strong performance in international markets. On one hand, the slowdown in its most important consumer base is concerning. However, PepsiCo still maintains a highly dominant position globally and boasts a healthy balance sheet. These fundamentals suggest that the company has the resources and strategic flexibility to turn the story around, creating a potential opportunity for investors.

Investor Pressure for Change

The disconnect between PepsiCo's high-quality business— backed by iconic brands, massive scale, and a powerful global distribution network—and its current performance and market valuation has not gone unnoticed. In September, Elliott Management, a prestigious investment management firm, announced their large holdings of PepsiCo stocks and announced plans to present a proposal to management. The proposal aims to implement strategic changes designed to enhance operational performance and unlock shareholder value.

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Elliott's proposal focuses on three key initiatives across PepsiCo's business lines.

First, Elliott urges management to review PepsiCo's brand portfolio and product lineup, which they consider overly complex and oversized. According to their assessment, many products add operational costs without generating meaningful revenue, ultimately weighing on topline growth and eroding profit margins.

Second, Elliott advocates for spinning off PepsiCo's bottling operations. The rationale is that adopting a franchisor–franchisee model would enable PepsiCo to concentrate resources on its high-margin core business—managing and monetizing its brands—while outsourcing the asset-heavy, lower-margin, and operationally demanding bottling activities. This approach would effectively replicate Coca-Cola's business model, which has proven successful in driving efficiency and profitability.

Third, Elliott proposes that the additional cash flow generated from a more efficient operation and a streamlined product portfolio should be reinvested into growth initiatives. These include advancing technology, strengthening marketing efforts, and acquiring emerging brands and innovative products to keep PepsiCo competitive.

Since Elliott expressed its intention to influence PepsiCo's strategy, CEO Ramon Laguarta stated that discussions between the fund and company executives had been constructive. On December 8, PepsiCo announced an agreement with Elliott to adopt virtually all of the strategic changes outlined by the fund. Notably, Elliott will not receive a seat on PepsiCo's board of directors, and there are no plans for a proxy contest.

In our view, the news are positive for Pepsi, and we believe the agreement with Elliott will serve as a catalyst for meaningful strategic transformation. While implementation—particularly the divestiture of bottling operations—will take time, these changes are designed to strengthen margins, simplify operations, and unlock long-term growth. The proposed initiatives are designed to strengthen the company's financial performance and operational efficiency. Collectively, these measures aim to increase profitability, streamline processes, and optimize resource allocation. By freeing up capital, the company can reinvest strategically in its most promising business segments, ensuring sustainable growth and long-term competitiveness.

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