



# PepsiCo, Inc (PEP)

Updated April 5<sup>th</sup>, 2018 by Nate Parsh

## Key Metrics

<b>Current Price:</b> \$111	<b>5 Year CAGR Estimate:</b> 6.5%	<b>Quality Percentile:</b> N/A
<b>Fair Value Price:</b> \$108	<b>5 Year Growth Estimate:</b> 4.0%	<b>Momentum Percentile:</b> N/A
<b>% Fair Value:</b> 103%	<b>5 Year Valuation Multiple Estimate:</b> -0.5%	<b>Total Return Percentile:</b> N/A
<b>Dividend Yield:</b> 3.0%	<b>5 Year Price Target</b> \$131	<b>Valuation Percentile:</b> N/A

## Overview & Current Events

Pepsi is a global food and beverage company that had more than \$63 billion in sales in 2017. The company's products include Pepsi, Mountain Dew, Frito-Lay chips, Gatorade, Tropicana orange juice and Quaker foods. The company has 23 \$1 billion brands in its portfolio. Pepsi was founded in 1898 and currently employs 264,000 people around the world.

Pepsi reported 4<sup>th</sup> quarter earnings for 2017 on 2/13/2018. Adjusted EPS was \$1.31, an \$0.11 increase from Q4 2016, while sales grew 0.1% to \$19.5 billion. Over the past 16 quarters, Pepsi has surpassed or produced an inline EPS figure every quarter. The company has only failed to grow sales just twice during this time. Pepsi had 2.3% organic sales growth in the 4<sup>th</sup> quarter. The company's two largest divisions saw sales decline during the quarter, with North American Beverages falling 6% and Frito-Lay North America dropping 1%. International sales grew 6.6% in Q4.

## Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
<b>EPS</b>	\$3.21	\$3.77	\$3.91	\$3.98	\$3.92	\$4.37	\$4.27	\$4.66	\$4.85	\$5.23	<b>\$5.70</b>	<b>\$6.93</b>
<b>DPS</b>	\$1.60	\$1.75	\$1.89	\$2.03	\$2.13	\$2.24	\$2.53	\$2.79	\$2.96	\$3.12	<b>\$3.47</b>	<b>\$4.16</b>

Pepsi has grown earnings at a rate of 4.2% per year from 2010-2017. Pepsi's growth over this time period came from sales growth (~1.5%), margin improvements (~1%), and share repurchases (~1.5%). We expect sales to continue growing at between 1% and 3% per year going forward, with share repurchases and margin gains adding another 1% to 3% to growth. This comes to an expected growth rate of 4% at the median.

With that said, Pepsi is expecting stronger growth in fiscal 2018. The company is expecting to earn \$5.70 per share in 2018, 9% growth from last year.

Pepsi has raised its dividend for the past 46 years and the average increase over the past 10 years is 8.9%. The company announced on 2/13/2018 that the dividend would be raised 15.2% for the June payment. Pepsi has historically raised the dividend on the third payment of the year (the company pays a dividend in January, March, June and September). We expect Pepsi's dividend payout ratio to remain at 60% out to 2023, which implies \$4.16 in DPS by that time.

## Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
<b>Avg. P/E</b>	20.5	14.7	16.5	16.4	17.4	18.4	20.8	20.7	21.4	21.7	<b>19.4</b>	<b>18.9</b>
<b>Avg. Yld.</b>	2.4%	3.2%	2.9%	3.1%	3.1%	2.8%	2.8%	2.9%	2.9%	2.7%	<b>3.0%</b>	<b>3.1%</b>

Post-recession, Pepsi's P/E has expanded, though gradually over time. The average P/E over the past 10 years is just slightly below the expected multiple for 2018. This means that the stock is just slightly overvalued based off of its recent history.

Pepsi's current dividend yield is above the S&P 500 and 10-year Treasury Bond. The company also has one of the longest dividend growth streaks in the market and just gave investors an above average dividend increase for the upcoming payment. With an expected payout ratio of 61% for 2018, Pepsi has room for continued dividend growth going forward.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
<b>GP/A</b>	63.6%	58.1%	45.9%	47.9%	45.8%	45.4%	50.3%	49.3%	47.1%	43.5%	<b>43%</b>	<b>47.1%</b>
<b>Debt/A</b>	66.4%	57.8%	68.9%	71.8%	70.1%	68.7%	75.3%	82.7%	84.7%	86.2%	<b>87%</b>	<b>79.5%</b>
<b>Int. Cov.</b>	25.6	25.7	10.9	12.1	11.4	12	11.7	9.2	8	11.9	<b>11.6</b>	<b>10.6</b>
<b>Payout</b>	49.8%	46.4%	48.3%	51%	54.3%	52.5%	59.3%	59.9%	61%	59.7%	<b>60.9%</b>	<b>60.0%</b>
<b>Std. Dev.</b>	32.1%	22.8%	15%	17.3%	10.6%	13.5%	12.9%	15.2%	13.5%	9.8%	<b>11.1%</b>	<b>16.3%</b>

Pepsi is a relatively recession proof company. EPS grew at the height of the last recession and the stock often offers a very generous dividend yield. While debt has climbed higher in recent years, the company is expecting \$6 billion in cash flow in 2018. Pepsi often generates more cash flow than its competitors, so the company can use this capital to pay down existing debt while still returning cash to shareholders.

While known for their carbonated beverages, Pepsi's food and snacks make up approximately 52% of sales. Pepsi's line of "Better for You" offerings are designed to meet consumers' desire for healthier food and drink options. These items had double digit growth during 2017. Products with less than 70 calories from added sugar make up ~45% of sales.

### Final Thoughts & Recommendation

Shareholders of Pepsi have the potential to see returns of 6.5% per year through 2023. This estimate is based off a combination of growth (4%), dividends (3%) and multiple mean revision (-0.5%). Pepsi's long dividend history, stability, and general safety make it a reasonable hold for risk averse investors. With that said, Pepsi's expected total returns are not particularly high. Now is not the time to enter into a position in this iconic chip and beverage company.

### Total Return Breakdown by Year

