

## PepsiCo & Coca-Cola Company: Vertical Integration

On August 4, 2009, Indra Nooyi (CEO of PepsiCo) invited Ira Hall, director of Pepsi Bottling Group (PBG), to her home. Nearly four months had passed since PepsiCo (herein referred to as Pepsi) began its campaign to acquire its two largest independent bottlers, PBG and PepsiAmericas. It seemed that the negotiations had collapsed when the two parties met in Pepsi's Westchester, New York, airplane hangar in July. But this time Hall, negotiating on behalf of both PBG and PepsiAmericas, and Nooyi struck a deal. At \$36.50 a share, half in cash and half in stock, Pepsi brought its two largest bottlers in-house.<sup>1</sup> Nooyi later told reporters that the independent franchise bottling model in North America was a "relic of the past."<sup>2</sup>

Immediately after the acquisition, Coca-Cola Company (herein referred to as Coke) rejected Pepsi's strategy. CEO Muhtar Kent asserted that he "fundamentally believe[s] that the franchise model in its broadest sense is the best way to win in the marketplace."<sup>3</sup> Yet six months later, Coke purchased the North American operations of its largest bottler, and Kent confidently declared, "Our new North American structure will create an unparalleled combination of businesses, which will serve as our passport to winning in the world's largest nonalcoholic ready-to-drink profit pool."<sup>4</sup>

With these acquisitions, the two industry leaders changed the structure of the carbonated soft drink (CSD) industry in North America. The former CEO of Pepsi Bottling Group, who became the CEO of Pepsi's new in-house bottling operation (Pepsi Beverages Company), declared that Coke's decision "confirms that this is the right move, the right strategy, the right model for North America."<sup>5</sup>

### Introduction

Pepsi's highly publicized bottler acquisitions followed by Coke's subsequent adoption of the same strategy raises several questions: 1) Is the current strategy of forward integration into bottling appropriate for the two companies? 2) Was the previous strategy involving franchised bottlers appropriate for its time? 3) What has changed in the industry to cause this change in strategy?

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