

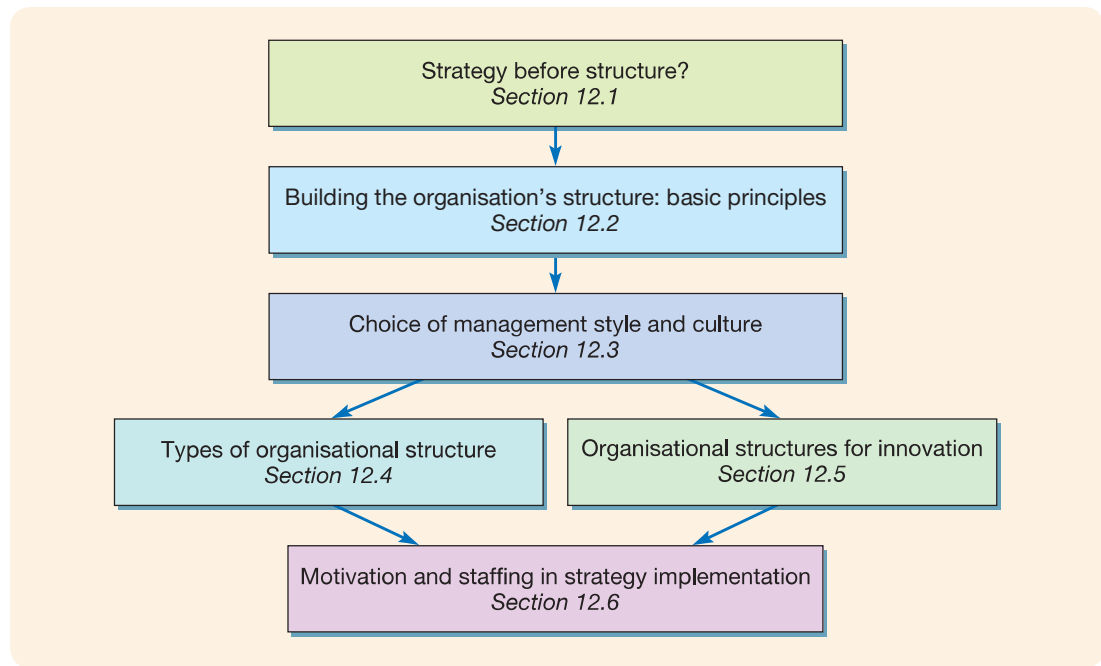


Figure 12.1 Organisation structure and people issues

CASE STUDY 12.1

PepsiCo: organising to integrate its acquisitions

Over a three-year period from 1998 to 2001, the US food and drink company PepsiCo made two major acquisitions. Each purchase was bought for a price premium that could only be repaid by finding new synergies and economies of scale. This required PepsiCo to develop new organisation structures designed to deliver these benefits in the years that followed.

Background – the company itself

PepsiCo is probably best known for its carbonated cola drink, Pepsi-Cola, which it sells in most countries around the world, often in second place to its great rival Coca-Cola. However, in terms of total sales, PepsiCo is actually much larger than Coca-Cola – sales of \$29 billion in 2004 compared with Coke's \$22 billion. The main reason for the greater size is that PepsiCo is also the world's largest snack and crisp manufacturer, with a series of brands in regions of the world – including Frito-Lay in North America and Walkers in the UK. However, the company also has some other famous brand names like Gatorade, Tropicana fruit juices and Quaker breakfast cereals. Table 12.1 sets out some of its leading products, including those that arrived through its acquisition strategy in the six years to 2004.

Company major acquisitions – Tropicana and Quaker

Both the Tropicana range of fresh fruit drinks and the Quaker range of products came from PepsiCo acquisitions in the period 1998–2001. Tropicana was bought from Seagram for \$3.3 billion in 1998 and Quaker for \$15 billion in 2001. In both

Table 12.1 PepsiCo's top ten products at retail prices

Brand	Worldwide sales (\$ bn)
Regular Pepsi	17.0
Diet Pepsi	6.0
Mountain Dew	5.5
Gatorade Sports Drink	5.2 Acquired 2001
Lays Potato Chips	5.0
Doritos Tortilla Chips	3.0
Tropicana Juice Drink	2.9 Acquired 1998
7Up Drink (outside the USA)	2.4
Aquafina bottled water	2.3
Cheetos Cheese Flavored Snacks	2.0
Quaker Cereals	1.5 Acquired 2001

Source: company report and accounts 2004.

cases, PepsiCo paid a significant premium over the asset book value of the companies. It took the view that there were significant synergies and economies of scale to be gained from these two acquisitions. With regard to Quaker, PepsiCo was particularly interested in the sports drink Gatorade, which delivered the market leader in a new and fast-growing segment of the beverage market. The same purchase came with the Quaker cereal range, which was under heavy competitive pressure from Kellogg and General Mills – see Case 2.1. However, the Quaker brand also brought the possibility of new snack products. PepsiCo then began to organise the company to exploit this advantage, not only in North America but also in Europe.

PepsiCo company re-organisation to exploit the full acquisition potential

Building on its strong competitive resources was the prime starting point in developing the revised organisation structure for PepsiCo. Such resources included its major network of contacts with supermarkets across North America and, to a lesser extent, other countries. They also included its existing brand franchises in names like Pepsi and Frito-Lay, Quaker, Gatorade and Tropicana. The company had a specialist distribution structure designed to deliver fresh and fragile snacks every week directly to 15,000 outlets across the USA and indirectly to around 500,000 outlets. It also had a strong network of bottlers who were responsible for delivering Pepsi. The company had a record of product and packaging innovation which came from its Pepsi and Frito-Lay technical development units, the Gatorade Sports Science Institute and the Tropicana Nutrition Center. All were skilled at developing new products and packaging. Such units were kept centrally at headquarters on behalf of all operating companies.

Because PepsiCo was particularly strong in North America in virtually every product category, it was decided to set up North American divisions and separate these from its other, international operations. In addition, although the sports drink Gatorade and the Quaker cereal products were important in North America, they had a more limited franchise internationally – especially Gatorade, which was largely unknown outside the American continent. It was decided to combine these product areas internationally with some of its other product groups.

PepsiCo main organisation structure – 2001

In 2001, PepsiCo therefore had the following organisational divisions, each reporting to headquarters:

- *Pepsi-Cola North America* was responsible not only for the largest brand but also for building a new product range of non-carbonated drinks such as bottled water. The company was not expecting this area to yield major savings from its two acquisitions. In 2004, this was combined with Tropicana/Gatorade – see below.
- *PepsiCo Beverages International* contained the combined international operations of Pepsi-Cola, Tropicana and Gatorade. It was planned to combine general and administrative functions



Faced with increased competition and slow growth, PepsiCo has responded by a strategy of moving into more rapidly growing markets – soft drinks, mineral water and snack products. But this has meant reorganising the company.

and gain 'very substantial cost savings'. One of the problems here was that, although the Pepsi brand was strong in the USA, its international brand share was weaker – especially in parts of Europe. It was therefore more cost-effective to combine it with Tropicana (Gatorade was too small to be important) and gain cost savings from shared overheads. In 2004, this was combined with Frito-Lay International – see below.

- *Frito-Lay North America* had part of the Quaker range of sweet cereal bars, energy bars and similar products, combined with its existing savoury crisps and snacks. The aim was to gain substantial cost savings and at the same time to offer the broader range of products to its existing outlets, thus increasing sales.
- *Frito-Lay International*. The snack and crisp products were sold across some 40 countries. The company already had some strong market positions, for example, 80 per cent of the Mexican snack market and 40 per cent of the UK snack market with Walkers Crisps. The aim here was to add the Quaker food distribution and gain major cost savings on distribution. The Quaker international cereal product range was also included in this area – probably because it was convenient and PepsiCo had to buy this product range in order to obtain Gatorade, as mentioned above. In 2004, this was combined with PepsiCo Beverages International.
- *Gatorade/Tropicana North America*. These two major product areas – sports drinks and fruit juices – were combined as a separate area from cola drinks because they were used and sold in different ways and through different outlets. More specifically, there was a common 'hot-fill' manufacturing process that could be used to deliver substantial cost savings. In 2004, this was combined with PepsiCo North America – see below.
- *Quaker Foods North America*. PepsiCo decided to keep the Quaker cereals and related products, like Aunt Jemima

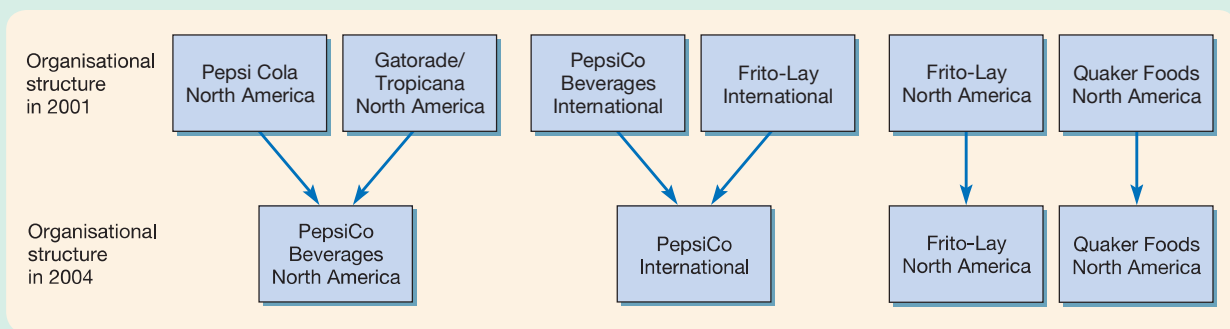


Figure 12.2 How PepsiCo re-organised in 2004

syrup and mixes, together in North America. Some commentators suspected that this separate division would also allow the product range to be sold more easily at some later stage – it simply did not fit with the main strengths of PepsiCo and faced strong competition in both North America and internationally. The well-established warehouse distribution capabilities of Quaker and Gatorade brought important new scale to a new delivery/distribution system for PepsiCo.

PepsiCo further re-organisation – 2004

By 2004, PepsiCo had decided to combine several of the above divisions – see Figure 12.2. The reasons for this change in organisation structure were:

- *PepsiCo Beverages International was combined with Frito-Lay International.* The new division was called PepsiCo International. The logic here was to build on the company's different international strengths in different international markets. For example, its snack brands were particularly strong in Mexico with the Sabritas brand, in the UK with the Walkers brand and in Australia with the Smiths brand. In other countries, Pepsi-Cola was stronger and the snacks brands were relatively weak. Whatever was the strongest product category would be the lead brand and would then support the other weaker brands. This could best be done if there was one organisation rather than separate organisations.
- *Gatorade/Tropicana North America was combined with Pepsi Cola North America for financial reporting.* The new division was called PepsiCo Beverages North America. The reasoning here was to allow the company to exploit its strengths in non-carbonated and healthy fruit drinks across a wider range of outlets. Coca-Cola was leader in the carbonated drinks market, but Pepsi with Tropicana and Gatorade was easily the market leader in the total soft drinks market. To exploit this leadership, it was essential to drive the various brands as part of one team. This was particularly important given the increased bargaining power of the large retail

supermarket chains like the world's largest retailer, Wal-Mart – PepsiCo Beverages became 'the No 1 liquid refreshment beverage company in measured channels'.

PepsiCo organisation in 2010

Like many other organisations, the company re-organised further over the years from 2004. The latest organisation structure is fully described in the report for 2010 but includes separate structures for Latin America, Europe and Asia, the Middle East and Africa as these parts have become more significant to the overall business of the company.



PepsiCo has an extensive range of activities associated with green strategy:

'Environmental initiatives help us identify business synergies and cut our operating costs. Equally important is improving efficiencies in packaging materials, water and energy use, so we may continue to minimize waste and move toward significant environmental goals . . .'

(PepsiCo, Inc. Annual Report 2010).

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Case questions

- 1 Why was PepsiCo essentially organised into North American and international divisions? Why were there some variations in this structure? Examining the organisation structures outlined in this chapter, in which category would you put PepsiCo?
- 2 What benefits was the company seeking from its acquisitions? How did the change in organisation structure contribute to such benefits? In order to achieve such benefits, what actions would have to be taken? Would they have any human consequences? If so, what?
- 3 What lessons, if any, on strategy and organisation structure can be drawn from the approach of PepsiCo in developing its new organisation structure?



Exploration of prescriptive and emergent perspectives in human resource analysis.