

The Trend of PepsiCo by Comparing PepsiCo's Financial Reports in 2018 to 2019 Based on Harvard Analytical Framework

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ABSTRACT

The proposal of Harvard analytical framework makes non-financial information gradually attract people's attention. Besides, as a statement reflecting the financial status and operating results of an enterprise, financial reports can always accurately reflect the operating status and annual strategy of the enterprise. They can also reveal the risks and expected profit of the enterprise, thus providing users with information to make decisions. Based on PepsiCo's publicly financial reports in 2018-2019, this paper uses the Harvard analytical framework to analyze PepsiCo's comprehensive financial status from four levels: strategy, accounting, finance and prospect. The dynamic and potential economic information is analyzed through the static statement, so as to further understand the company's operating situation and annual strategy and evaluate its potential opportunities and risks. Based on this assessment, the paper concludes that PepsiCo's performance in 2019 will be favorable and makes recommendations based on the risks identified in the analysis.

Keywords: *Harvard Analytical Framework, SWOT analysis, Analysis on the Financial Report, Financial Analysis, PepsiCo, Prospect Forecast*

1. INTRODUCTION

In today's unprecedentedly active market transactions, financial reports, as written documents reflecting the financial status and operating results of an enterprise, have received unprecedented attention for their indicative function of reflecting a company's performance [1]. However, the information obtained from traditional financial statement analysis methods such as ratio analysis (Williams) method and trend analysis method (Stephen) is not enough to fully support information users to make decisions. In the 21st century, three professors in Harvard namely K.G. Palepu, P.M. Healy and V.L. Bernard, were the first to put forward the new thinking in financial report analysis, the Harvard analysis framework. It mainly analyzes the company's financial statements from the perspectives of strategic analysis, accounting analysis, financial analysis and prospective analysis. The proposal of Harvard analysis framework makes the analysis of financial statements further improved by information users [2]. As one of the leading players in the soft drink market, PepsiCo's financial reports not only reflect the operating performance of the company in its particular fiscal year, but also reveal the underlying business information of the soft drink

market as a whole. The purpose of this paper is to make a comprehensive multi-angle analysis of PepsiCo's 2019 financial report by using the new financial report analysis method and comparing with its 2018 financial report, so as to make up for the shortcoming of unitary financial report analysis angle based on the traditional financial report analysis method. It is hoped that the examples analyzed in this paper can provide some feasible analysis methodology for subjects who need to read relevant information from financial statements.

2. ANALYSIS

2.1. Strategic Analysis

From the four perspectives of Harvard analytical framework, strategic analysis is the beginning of the financial statement analysis in Harvard Analysis framework, aiming at determining the main profit drivers and operational risks, and qualitatively evaluating the profitability of enterprises. In order to strive for comprehensive analysis and rigorous structure, this paper will also use SWOT analysis to

analyze PepsiCo' internal strengths, weaknesses and external opportunities and threats in the part of strategic analysis.

2.1.1. Strengths

Pepsi entered the market earlier than most of the other soft drinks companies, therefore it has a greater advantage in market operations [3]. In 2019, PepsiCo's global market penetration rate reached 22.7%. Moreover, as a mature company, the profit brought by the brand effect of PepsiCo can not be underestimated. Its strong innovation and product development capabilities have enabled PepsiCo to expand its products from soft drinks market to the entire food market, as well as the footwear and clothing market, which has further increased Pepsi's market share and expanded its brand influence. The brand propositions and personalities promoted by Pepsi, such as "eager to infinite", have huge market and loyal consumer groups among young consumer groups [4].

2.1.2. Weaknesses

Influenced by many factors, nowadays consumers' preferences in product selection have changed a lot. For example, the increasing attention people pay on health and the changing age structure of consumers caused by the aging of the population may shrink PepsiCo's market. Therefore, the market growth rate of Pepsi cola, the main product of PepsiCo, may face a downward trend, and the market demand may also decrease [5]. On the other hand, PepsiCo's large organization means higher management costs and control expenses, which will offset the profits made by PepsiCo to some extent.

2.1.3. Opportunities

With 140,000 employees in more than 200 countries, PepsiCo is the world's fourth-largest food and beverage company with annual sales of \$27 billion. In 2005, PepsiCo's "This is Pepsi" end revolution created the perfect sales point. In doing so, Pepsi has further expanded its markets around the world. Thanks to the tide of economic globalization, Pepsi has obtained opportunities in many overseas markets, but such opportunities and huge

market gap are beyond the satisfaction of the domestic market and the single soft drink market [6]. In addition, PepsiCo is making significant progress in sustainability journey to catalyze change and help build a more sustainable food system that can meet 21st century needs [7]. This will give PepsiCo more opportunities to cooperate with the government and has a positive impact on Pepsi's brand image.

2.1.4. Threats

Although PepsiCo is a century-old company, its main product, Pepsi-Cola, has always been threatened by Coca-Cola [8]. In addition, because of the profitability of Pepsi and Coca-Cola in the Cola market, new competitors may enter the barrier. In the green environment, the main form of packaging (such as plastic bottles, cans, etc.) of Pepsi's products may bring negative effects such as tax increase.

2.2. Accounting Analysis

On the basis of strategic analysis, accounting analysis aims to evaluate the extent to which accounting reflects the basic operating reality.

2.2.1. Accounting Policies

As a famous listed company, PepsiCo is supervised and required by NASDAQ and other relevant institutions, therefore the integrity, authenticity and accuracy of its data and annual reports are largely guaranteed. Its financial disclosure and information disclosure also have high reliability and credibility. In its annual report disclosure of accounting policies, for investment, assets of revenue recognition contract, lease, revenue recognition, foreign currency, taxes, welfare costs, government support, borrowing costs, property, plant and equipment, intangible assets, asset impairment, inventory, provision for bad debt and financial tools and other major accounting policies are carried on the detailed instructions. Compare the accounting policies with other same type companies, there is no obvious difference.

2.2.2. Cash flow

Table 1. Summary of Operations of PepsiCo in 2018&2019 [9].

Year	2019	2018
Net Cash Provided by Operating Activities	\$ 9,649	\$ 9,415
Net Cash (Used for)/Provided by Investing Activities	\$ 6,437	\$ 4,564
Net Cash Used for Financing Activities	\$8,489	\$ 13,769
Net (Decrease)/Increase in Cash and Cash Equivalents and Restricted Cash	\$5,199	\$112
Cash and Cash Equivalents and Restricted Cash, Beginning of Year	\$10,769	\$10,657
Cash and Cash Equivalents and Restricted Cash, End of Year	\$ 5,570	\$ 10,769

It can be seen from the table that in 2018, net cash provides by Operation is \$9,415, which is \$9,649 in 2019. It is obviously that PepsiCo's operating activities in 2019 provide the company with more cash flow than that in 2018, which may mean that PepsiCo gains more profits in 2019, or that PepsiCo's transactions in 2019 are more paid in cash, while the revenue is reduced in the form of accounts receivable. Generally speaking, this situation indicates a success of PepsiCo's operating activities in 2019.

Besides, the cash flow in investing activities of PepsiCo in 2019 is negative, which is -\$6,437. One possibility is that Pepsi failed to make an investment in 2019 and the costs are more than profits; it could also indicate that PepsiCo has invested in one or more new projects in 2019.

In terms of financing activities, the cash flows in 2018 and 2019 are both negative, which is -\$8,489 and -\$13,769 respectively. It indicates that PepsiCo has carried out a large number of debt-paying and profit distribution activities in 2018 and 2019. It is also possible that the enterprise has sold certain assets and used the gain from disposal on financing activities.

The cash flow of 2019 has increased compared with that of 2018, which may indicate that PepsiCo has obtained more capital inflows through the form of stocks or bonds in 2019. This phenomenon may be related to the expansion of the company's operation scale or the development of new production lines.

From the other side, compared with the end of 2018, the amount of cash and cash equivalents and restricted cash was down about 48% in the end of 2019, although this can be explained by the active degree is high, PepsiCo's cash source is abundant and the management of cash flow is good, but may also be the potential risk that cash is in short supply.

2.3. Financial Analysis

Financial analysis aims to evaluate the company's operating capability through some financial data and indicators.

2.3.1. Solvency analysis

Table 2. Consolidated Balance of PepsiCo, Inc. and Subsidiaries in December 28, 2019 and December 29, 2018 [10].

Year	2019	2018
Total Current Assets	\$ 17,645	\$ 21,893
Total Assets	\$ 78,547	\$ 77,648
Total Current Liabilities	\$ 20,461	\$ 22,138
Total Liabilities	\$ 63,679	\$ 63,046

According to the table, the total assets in 2019 is \$78,547, which in 2018 is \$77,648. The total liabilities in 2019 is \$63,679, and in 2018 is \$63,046.

$$\text{Debt to asset ratio (2019)} = \$63,679 / \$78,547 = 81.07\% \quad (1)$$

$$\text{Debt to asset ratio (2018)} = \$63,046 / \$77,648 = 81.19\% \quad (2)$$

Compared with 2018, the trend is down. From the standpoint of creditors, this is a good trend, which represents a small decline in the corporate risks that creditors have to bear, an improvement in the corporate debt paying ability, and a decrease in the corporate financing risks. From the perspective of investors, on the premise that the profit rate of all capital is higher than the interest rate of borrowed capital, investors hope that the index will rise in order to obtain higher income. From the perspective of operators, excessive amount of debt is difficult to finance, and the decline of this index will facilitate

enterprises to borrow more funds and expand the market to improve profits and solvency.

$$\text{Current ratio (2019)} = \$17,645 / \$20,461 = 86.23\% \quad (3)$$

$$\text{Current ratio (2018)} = \$21,893 / \$22,138 = 98.89\% \quad (4)$$

Generally speaking, companies are more stable when the current ratio is close to 2. However, whether in 2018 or 2019, Pepsi's current ratio is far below 2. Considering the actual situation of Pepsi, one possibility of this situation is that PepsiCo's cash source is abundant and well managed, so it does not need to reserve a large amount of capital. It may also be that PepsiCo is keeping a good control on the growth rate of accounts receivable and inventory. The downward trend in current ratio reflects the fact that PepsiCo's inventory backlog in 2019 is likely to exceed that in 2018, with reduced liquidity of cash flow and the risk of a decline in short-term solvency.

2.3.2. Profitability analysis

Table 3. Consolidated financial data of PepsiCo in 2018&2019 [11].

Year	2019	2018
Net revenue	\$ 67,161	\$ 64,661
Provision for/(benefit from) income taxes (a)	\$ 1,959	\$ 3,370
Net income attributable to PepsiCo (a)	\$ 7,314	\$ 12,515
Net income attributable to PepsiCo per Common share–basic (a)	\$ 5.23	\$ 8.84
Net income attributable to PepsiCo per Common share–diluted (a)	\$ 5.20	\$ 8.78
Cash dividends declared per common share	\$ 3.7925	\$ 3.5875

(a)2019 and 2018 results included the impact of the TCJ Act. Additionally, 2018 results included other net tax benefits related to the reorganization of PepsiCo's international operations.

It can be seen from the table that PepsiCo had net revenue \$67,161 in 2019, which is \$64,661 in 2018. It indicates that PepsiCo had higher net income in 2019 than that in 2018. Besides, net income attributable to PepsiCo is significantly lower than that in 2018, indicating that the return generated from PepsiCo investment is lower than that in 2018. This situation supports that the information that in the accounting analysis, according to the cash flow statement for investment activities of cash expenditure was increasing compared. This suggests that PepsiCo's new investment choice in 2019 may be failure. In addition, another possibility is that PepsiCo was develop new investments in 2019, and the project has not yet reached the stage where it can recoup the money. But overall, the cash dividends per common share rose in 2019 compared with 2018, meaning the price on PepsiCo's shares was increased and the total profit was higher than 2018. In other words, although PepsiCo may fail in investment activities in 2019, its overall operation is still better than 2018, and its overall profitability has also improved. Therefore, the profitability of PepsiCo is still reliable and stable.

2.4. Prospect Analysis

Prospect analysis mainly emphasizes the possible trends of the company.

2.4.1. Prospects for Development

In the face of rapid market changes and fierce competition, Pepsi should make full use of big data, effectively organize internal management and external suppliers, and quickly respond to project time and cost budgeting [12]. This will save PepsiCo more operating expense and offset the negative impact that may be caused by the decrease of cash holdings that analyzed in accounting analysis and financial analysis.

In addition, in nowadays' economic globalization, multinational companies have accelerated the process of internationalization, and PepsiCo may also try to seize the opportunity to rapidly develop and expand overseas markets and actively promote the localization of products, which can also help PepsiCo to increase the global market share. From this point of view, Pepsi is also likely to gain more opportunities and greater profits in overseas markets in the future. From the perspective of long-term development, the development prospects of PepsiCo in overseas markets are undoubtedly potential.

Besides, in view of Pepsi's excellent solvency and profitability, PepsiCo may further increase the cash flow used for investment in the future, which may also be an opportunity for Pepsi's profitability, but may also be a potential risk.

2.4.2. Risk Prediction

As mentioned above, with the development of the concept of green and healthy, PepsiCo's main products are facing the risk of a decline in market demand. At the same time, the concept of sustainability has also influenced Pepsi's brand image. The development of new products that cater to the market and the transformation of corporate image not only require a lot of funds, but also will face great risks and market uncertainty. These potential risk factors are likely to affect PepsiCo's operating performance and profitability in the new quarter.

3. CONCLUSION

It can be seen from the analysis of Harvard analytical framework that the current operation capacity, development space and prospect of PepsiCo are very reliable. The company has sufficient sources of funds, good internal management and control, and stable and excellent solvency and profitability. Compared with 2018, the majority of indicators for 2019 showed a positive trend. In addition, PepsiCo has also been actively exploring overseas markets to obtain more opportunities, and has achieved some success at this stage [13].

In order to deal with the concept of sustainable development and the concept of green and health, it is suggested that PepsiCo put forward the green development goal next year to build a positive brand image. PepsiCo can also develop new products to meet diversified market demands.

However, the Harvard analytical framework used in this paper also has some shortcomings. Harvard analytical framework is more about analyzing a company's ability and potential from the perspective of operational data. However, a company's strengths and weaknesses are not only reflected through data. Non-data indicators, such as employee enthusiasm and corporate culture, also play an important role in the growth of a company. When the analysis of a company combines the Harvard analytical framework with non-data factors, the understanding of a company can be more complete and more accurate.

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