



*Jesse Bross*

## **Elliot and the Pepsi Problem**

Yale Mergers and Acquisitions Club

Fall 2025 Consumer Report

On September 2, 2025, activist hedge fund Elliot Investment Management delivered a letter to the board of directors of PepsiCo. The letter mentions that Elliot has recently acquired a \$4B+ stake in the company, and believes in the future of PepsiCo as a business, calling Pepsi a storied “CPG bellwether.” Despite this, Elliot’s letter offers a scathing critique of PepsiCo’s recent management. They write that despite the company’s strong potential, “strategic and financial challenges have recently led to poor operational results, sharp stock-price underperformance and a meaningfully discounted valuation.”

According to Elliot, this problem was an avoidable one. The letter acknowledges recent problems in consumer sentiment and weakness in Pepsi’s snack offerings, but argues that the recent macro shift in consumer sentiment has not *caused* but *revealed* the underlying weakness in Pepsi’s business. Elliot claims that the strength in past years of Pepsi Foods North America (PFNA), has obscured top and bottom line weakness in PepsiCo Beverages North America (PBNA). With recent PFNA underperformance however, the underlying mismanagement of PBNA has been revealed. For Elliot, PBNA poor performance comes down to a vertically integrating bottling process which has weakened margins, in conjunction with an unfocused product slate hindering revenue growth. PFNA is not beyond critique for Elliot as well, where they see potential for a divestiture of underperforming Quaker brands combined with a pullback in misallocated capital expenditure which didn’t properly estimate demand for salty foods and snacks.

Elliot’s letter argues there exists 50+% share price upside if their proposed changes were to take effect. This would derive from an increase in revenue, improved margin profile, and slight multiple uplift. Following the release of the letter, PepsiCo stock declined. Since the initial September slump, it has seen a slight rise and fall, but the stock is largely flat since Elliot’s plan was unveiled. In December, Elliot reached an agreement with Pepsi’s board in which Elliot would remain in contact with the board and PepsiCo would cut PFNA spend and reduce product offerings by 20%. Notably, as the FT mentions, the deal “does not commit to outsourcing soda distribution operations to independent bottlers, following in the footsteps of rival Coca-Cola, nor does it include a commitment to divestiture.”

As part of the Yale M&A Club, my goal in researching Elliot’s activist position was to understand whether the proposed divestitures and refranchising were compelling strategic spin off changes. Over the course of my research, Elliot has publicly agreed to not pursue such strategies and is content with only the strategic changes initially described in its letter and 75-page slide deck. Just because this agreement has been reached however, does not mean Elliot may not try to engage these ideas again. But perhaps Elliot abandoned these suggestions because they never made sense in the first place? I argue the

problems with PepsiCo are largely beyond Pepsi's control, and as such Elliot's activist thesis is ultimately a sign of wishful thinking in a situation largely dictated by external factors.

### **The Reality of Consumer Companies and Activists**

The Enchiridion by Epictetus begins with the lesson that "Some things are in our control and others not." While a quip often associated with the Stoics, it is quite fitting for understanding how investors ought to evaluate consumer businesses. The consumer landscape is extraordinarily unpredictable. One day Labubu may be the hottest new thing, and the next it may be irrelevant. When the change will come, no one can foresee. This is not to say that there is no place for strategy to help turn around consumer businesses. As the recent case with Abercrombie and Fitch shows, clear and focused leadership can be the key behind what drives the success of a consumer brand. The question Elliot must answer with PepsiCo is whether Pepsi's recent underperformance is in its control or out of its control. The answer of course, is that it is a little bit of both, but that still begs the question whether the portion within Pepsi's control is meaningful enough to drive the kind of equity return Elliot hopes for.

Activist investors have struggled in recent years to produce the kinds of returns they once did. While the strategy once succeeded in an era characterized by an underperforming and risk-averse management class, modern management teams are more aware of the threats from activists and LBOs. They realize that if they are doing a poor job with their business, the likes of Marc Steinberg and Jesse Cohn can swoop in and argue it's time for them to go. As such, one should be skeptical about whether Elliot's strategic proposals can actually drive meaningful value. Based on the reaction of the stock price, the market seemed skeptical as well. Let us consider the various proposals by Elliot, and I will explain why they may drive less value than one may think...

### **PBNA Refranchising: Structural Fix or Cyclical Distraction?**

One of the primary proposals from Elliot involves a refranchising of PBNA's bottling business. Right now, the bottling process for Pepsi's beverages is owned and operated by Pepsi. This is in contrast to competitors like Coca-Cola, who have outsourced the process and possess improved margins because of it. A refranchising would involve a switch to the Coke model, once in the past adopted by Pepsi. There are clear benefits from doing this. Refranchising would reduce capital intensity, improve reported operating margins, and potentially smooth free-cash-flow volatility for Pepsi. This would

allow Pepsi to focus on branding, product innovation, and marketing instead of a vertically integrated process.

Although Elliot's proposal seems convincing, the question is what has caused PBNA to struggle in the first place? Has the issue been margin, or sales overall? In the attached model, I have included a section which shows a breakdown of revenues and operating profits by segment. As one can see, PBNA top line growth has slowed from nearly 12% in 2021 to almost nothing in 2024. This at the same time that operating margin has stayed flat around 8-9%. Ultimately, PBNA's struggles have not been due to the bottling business, but rather because Pepsi's beverages have been underperforming. Carbonated soft drinks continue to face secular volume pressure, while growth categories such as energy drinks, functional beverages, and flavored waters are highly competitive and fragmented. Refranchising changes the cost structure of distribution, but it does not alter consumer preferences, pricing elasticity, or category mix.

### **PFNA Proposal: Investment Pullback and Asset Sales**

Let us turn to Elliot's proposal for PFNA. Several years back, PFNA had been outperforming PBNA growth in a meaningful way. Given this, high spend was put into foods, which for Pepsi consists of its FritoLay and Quaker brands. FritoLay is largely composed of salty snacks, whereas Quaker includes dry foods like cereals. Recent changes in consumer trends have however caused stalling growth for PFNA. With the increasing prevalence of GLP-1 drugs, demand for FritoLay has diminished. This, combined with increasingly health conscious North American consumers, have made FritoLay's offers far less appealing. Quaker has also struggled with a number of underperforming brands, according to Elliot's report.

Elliot's proposal for PFNA can be viewed in two parts: a pullback in investment from PFNA as a whole and a potential sale of underperforming assets. The pullback in investment is something Pepsi has been pursuing for some time. As mentioned, they had overly committed to snacking as a category, and have not seen recent returns from their high investment in FritoLay. Recognizing these secular trends, Pepsi has closed manufacturing plants and lines. CEO Ramon Laguarta said, "We will take the money we save here and put it back into portfolio expansion, affordability and driving growth." This was part of the December agreement struck between Elliot and PepsiCo, in which Pepsi agreed to continue this pullback in PFNA.

This leaves the second of Elliot's proposals, which is noticeably missing from the agreement: PFNA asset sales. In their 75-page report, Elliot calls for Pepsi to "streamline the portfolio by selling non-core assets that have either weighed on growth and/or margins, or serve as a distraction." They see this as a catalyst for restarting a PFNA growth flywheel, one which includes getting money from asset sales and using it on potential bolt on M&A (elaborated on below) to drive revenue growth. In particular, they single out Quaker as an underperforming asset for Pepsi and hint at a divestiture of Quaker on slide 58 of their presentation.

### **Bolt on M&A and a Quaker Sale**

The model attached to this article includes a valuation of Quaker based on a comps analysis, which given its lower growth rate would have Quaker trading far below FritoLay. However, if one examines FritoLay, it has also been slowing for the consumer trend reasons mentioned above. Even with Quaker sold, this begs the question of what Pepsi would actually do with the proceeds from the sale of Quaker. It seems Elliot is suggesting potential M&A for product innovation, but for M&A to make a significant difference for Pepsi they would have to purchase quite a large brand. Purchasing many individual brands involves integration risks, and Pepsi can't suddenly go from having a distribution network built for Fritos and Mountain Dew and suddenly leverage that same network to distribute whatever new high growth CPG product they deem attractive. While easy to include on a slide deck, the question is whether Pepsi can actually engage in effective bolt-on M&A. The Elliot report mentions "product innovation" and a "reconsideration" of Pepsi's offerings but says little of what this innovation will actually look like.

Ultimately, this begs the question of what PFNA's actual problems are. If the real issue is that consumers are no longer interested in buying Lays Chips and Fritos in the same quantity they once did, it's not clear how a sale of Quaker or the decommissioning of a few manufacturing plants (something Pepsi is already committed to doing) will be enough to drive the 50% return Elliot seeks. In my view, the real problem for PFNA is that consumers don't want PFNA's products in the way they once did. One could argue that this is a secular trend, but if GLP-1's prove to be effective and are truly the drive behind the slowing of FritoLay, I am unsure if this is simply an unavoidable macro headwind. Elliot's changes may help, but they can't fundamentally change Pepsi or the consumer segment they target.

### **Pepsi's Problems are Bigger than Strategy**

Elliot's recent agreement omits two of their major proposals from the initial activist thesis. The first is the refranchising of the bottling business for PBNA, and the second is the potential divestiture of Quaker and additional bolt-on M&A for PFNA. Elliot claimed that this approach, combined with cost-cutting and "reviewing" Pepsi's offerings to create a more "focused" portfolio of brands could drive a 50% equity return. The attached model shows how earnings would change with the various proposals. One can see that the sale of Quaker would actually be dilutive given its slow growth, and would actually cause a slight share decline if the cash were used to pay down debt. Ultimately, Pepsi's share price has been punished due to issues with their top line, not only their bottom line. While improved margins are always a positive for a business, in the case of Pepsi they are not enough for the company to look as attractive as it once did to investors.

But what about M&A? After all, this is the Yale M&A club and the aspect of Elliot's activist pitch which initially intrigued me that it would include the potential sale of large parts of Quaker and bolt-on M&A to drive top line growth. The question however is what would Pepsi actually pay for that top line growth? If they want high growth and trendy products, it means they are going to have to pay many more turns of EBITDA for those products than their own shares are valued at. Consider PepsiCo's recent acquisition of Poppi. Though not publicly available, online estimates indicate that Pepsi paid somewhere from 3-4x revenue in their \$2B purchase of Poppi. Pepsi itself on the other hand is only worth around 2x its annual revenue. No one can doubt that Poppi is a great addition to Pepsi's portfolio of brands, but M&A always begs the question of at what cost the addition comes? This is a large reason why M&A is extremely difficult as a solution to growth problems. According to a recent article by Fortune, over the past 40 years, 70-75% of M&A deals "fail." It turns out it is extremely difficult for M&A to be effective as a driver of growth.

When one considers the issues with PepsiCo, they don't lie in managerial issues. The issues impacting Pepsi are affecting the sector as a whole. Pepsi's core products (soft drinks, salty snacks, cereals, etc.) are becoming less popular with consumers. No amount of cost-cutting or bottling refranchising can solve that problem. This is not to say Elliot's proposals won't drive value, but in the case of Pepsi, Epictetus' first lesson is quite apt.

## Appendix: Models

Figures in millions

Revenue	2020	2021	2022	2023	2024
<b>Total</b>	<b>70372</b>	<b>79474</b>	<b>86392</b>	<b>91471</b>	<b>91854</b>
<i>Growth</i>	<i>N/A</i>	12.9%	8.7%	5.9%	0.4%
<b>PBNA</b>	<b>22559</b>	<b>25276</b>	<b>26213</b>	<b>27626</b>	<b>27769</b>
<i>Growth</i>	<i>N/A</i>	12.0%	3.7%	5.4%	0.5%
<b>Frito Lay NA</b>	<b>18189</b>	<b>19608</b>	<b>23291</b>	<b>24914</b>	<b>24755</b>
<i>Growth</i>	<i>N/A</i>	7.8%	18.8%	7.0%	-0.6%
<b>Quaker Foods NA</b>	<b>2742</b>	<b>2751</b>	<b>3160</b>	<b>3101</b>	<b>2676</b>
<i>Growth</i>	<i>N/A</i>	0.3%	14.9%	-1.9%	-13.7%

Operating Profit Before Tax	2020	2021	2022	2023	2024
<b>Total</b>	<b>10080</b>	<b>11162</b>	<b>11512</b>	<b>11986</b>	<b>12887</b>
<i>Operating Margin</i>	14.3%	14.0%	13.3%	13.1%	14.0%
<b>PBNA</b>	<b>1937</b>	<b>2442</b>	<b>5426</b>	<b>2584</b>	<b>2302</b>
<i>Operating Margin</i>	8.6%	9.7%	<i>N/A</i>	9.4%	8.3%
<b>Frito Lay NA</b>	<b>5340</b>	<b>5633</b>	<b>6135</b>	<b>6755</b>	<b>6316</b>
<i>Operating Margin</i>	29.4%	28.7%	26.3%	27.1%	25.5%
<b>Quaker Foods NA</b>	<b>669</b>	<b>578</b>	<b>604</b>	<b>492</b>	<b>303</b>
<i>Operating Margin</i>	24.4%	21.0%	19.1%	15.9%	11.3%

Quaker Foods NA (FY 2024 Figures)	
Revenue	2676
<i>Growth</i>	-13.7%
EBIT	303
<i>EBIT Margin</i>	11.3%
Tax Estimate	63.63
<b>NOPAT</b>	<b>239.37</b>
<i>NOPAT Margin</i>	8.9%

Proceeds from Quaker Sale	
NOPAT Multiple Estimate	11.0 x
EV (Quaker)	2633.07

Pro Forma PepsiCo (LTM Figures)	
Revenue	89690
EBIT	13555
<i>EBIT Margin</i>	15.1%
+D&A	3158
EBITDA	16713
EV/EBITDA	14.0 x
Pro Forma EV	234219.1

EV Equity Bridge	
Pro Forma EV	234219.1
Pro Forma Net Debt	39554.93
Market Cap	194664.2
<b>Pro Forma Share Price</b>	<b>141.06</b>
<i>Share Price Change</i>	-0.8%