BRYAN, GARNIER & CO

INDEPENDENT RESEARCH UPDATE

11th October 2016

AB InBev

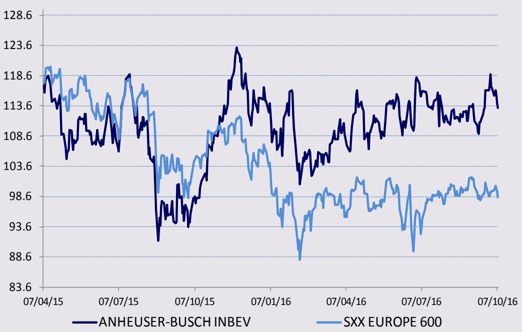
Fox in the Hen House

Food & Beverages

Fair Value EUR124 vs. 109 (price EUR115.05) **BUY vs. NEUTRAL**

Bloomberg	ABI BB
Reuters	ABI.BR
12-month High / Low (EUR)	123.3 / 98.4
Market capitalisation (EURm)	185,028
Enterprise Value (BG estimates EURm)	265,171
Avg. 6m daily volume ('000 shares)	1,420
Free Float	47.9%
3y EPS CAGR	6.3%
Gearing (12/15)	99%
Dividend yield (12/16e)	1.85%

YE December	12/15	12/16e	12/17e	12/18e
Revenue (USDm)	43,604	43,044	58,284	60,870
EBIT (USDm)	13,768	13,565	19,891	21,609
Basic EPS (USD)	4.96	3.58	5.55	6.10
Diluted EPS (USD)	5.10	4.52	5.58	6.12
EV/Sales	6.67x	6.87x	5.78x	5.47x
EV/EBITDA	17.2x	17.8x	14.1x	13.0x
EV/EBIT	21.1x	21.8x	16.9x	15.4x
P/E	25.2x	28.4x	23.0x	21.0x
ROCE	10.1	10.1	10.4	8.6



As the acquisition of SABMiller is finalised, there is already speculation on what the next target could be for AB InBev (AB InBev has an internal target to reach USD100bn in revenues by 2022). Although we believe that the case for Coca-Cola is stronger than that for PepsiCo, investors wanting to benefit from the transformation of AB InBev into a drinks company (from a brewer) are probably best to buy shares in AB InBev rather than those of any potential targets.

- Given the obvious strengths of AB InBev in cost-cutting and distribution, and the limited remaining possibilities in beer, consolidation in soft drinks might be the next step for the company. AB InBev would become a drinks business, rather than just a brewer, delivering more self-help with the potential cost and revenue benefits of selling beer and soft drinks through the same distribution system.
- Soft drinks and beer seem to have the same profile in terms of growth (i.e. 5% p.a. over the medium term), drivers (population growth, rising incomes and middle classes) and profitability (PepsiCo Beverages and the Coca-Cola system has operating margins of respectively 14% and 16%, which compares well with any brewer). However, AB InBev does better with an operating margin of 31% in beer and has already the credentials to do the same in soft drinks (Brazil's soft drinks margin of 44%).
- We believe that the case for The Coca-Cola Company is more convincing than that for PepsiCo, as Coca-Cola is the stronger soft drinks brand and has plenty of opportunities to drive share growth in still non-alcoholic beverages. Furthermore, it offers additional prospects of buying out the bottlers (which have been separated from the main company) at much lower valuations. Integrating the entire Coca-Cola system sets AB InBev on its way to USD300bn in revenues by 2030.
- We are increasing our 2017 operating profit and EPS by about 4% to take into account the resurgence of some emerging market currencies against the USD (ytd BRL +25%, ZAR +20%, COP+15%). Our DCF-based fair value of EUR124 is computed using a risk free rate of 1.6%, a risk premium of 7.0% and a Beta of 0.95.

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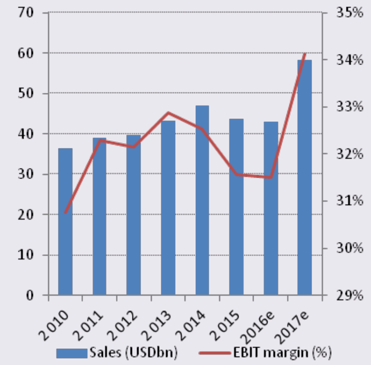

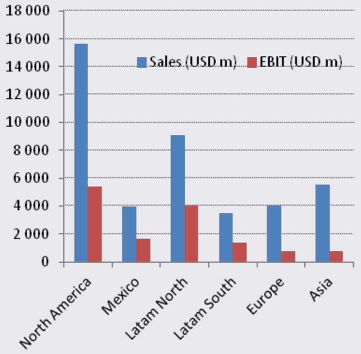

Company description

Anheuser-Busch InBev is the largest brewer in the world selling 408m hl (a 21% global market share) of beer and 50.8m hl of other beverages (soft drinks, water) in 2014. The company has a balanced portfolio with exposure to both mature markets (45% of 2014 EBIT) and developing markets (55%). Its main area of operations is North America (39% of EBIT) and Latin America (52%). AB InBev's brand portfolio comprises strong international and local brands including Budweiser, Bud Light, Stella Artois, Beck's, Skol and Brahma.

Income Statement (USDm)	**2013**	**2014**	**2015**	**2016e**	**2017e**	**2018e**
Revenues	43,195	47,063	43,604	43,044	58,284	60,870
Change (%)	*8.6%*	*9.0%*	*-7.3%*	*-1.3%*	*35.4%*	*4.4%*
Adjusted EBITDA	17,188	18,663	16,921	16,643	23,847	25,688
EBIT	14,203	15,308	13,768	13,565	19,891	21,609
Change (%)	*11.1%*	*7.8%*	*-10.1%*	*-1.5%*	*46.6%*	*8.6%*
Financial results	(2,203)	(1,319)	(1,453)	(3,989)	(3,539)	(3,483)
Pre-Tax profits	12,000	13,989	12,315	9,576	16,352	18,126
Exceptionals	(170)	(197)	136	0.0	0.0	0.0
Tax	(2,016)	(2,499)	(2,592)	(2,107)	(3,598)	(4,169)
Profits from associates	294	9.0	10.0	0.0	0.0	0.0
Minority interests	(2,124)	(2,086)	(1,594)	(1,492)	(1,679)	(1,793)
Net profit	7,984	9,216	8,275	5,978	11,076	12,164
Restated net profit	7,936	8,865	8,513	7,532	11,123	12,210
Change (%)	*10.2%*	*11.7%*	*-4.0%*	*-11.5%*	*47.7%*	*9.8%*
Cash Flow Statement (USDm)						
Operating cash flows	16,585	17,873	16,277	16,643	26,347	25,688
Change in working capital	866	815	1,337	(521)	724	2,298
Capex, net	377	(4,172)	(4,135)	(4,038)	(5,333)	(5,416)
Financial investments, net	(10,658)	(6,888)	(4,850)	0.0	(99,800)	0.0
Dividends	(6,253)	(7,400)	(7,966)	(7,415)	(10,001)	(10,861)
Other	(4,093)	(4,876)	(6,734)	(6,095)	34,510	(7,652)
Net debt	38,887	42,245	42,392	43,818	84,785	80,728
Free Cash flow	13,662	9,557	7,740	5,989	14,602	14,918
Balance Sheet (USDm)						
Tangible fixed assets	20,889	20,263	18,952	20,350	31,565	33,340
Intangibles assets	99,265	100,681	94,738	94,300	169,562	169,124
Cash & equivalents	10,239	8,877	7,074	7,074	7,074	7,074
current assets	9,896	11,551	12,476	8,644	13,174	12,660
Other assets	1,377	1,178	1,395	1,395	2,395	2,395
Total assets	141,666	142,550	134,635	131,763	223,770	224,594
L & ST Debt	49,126	51,122	49,466	50,892	91,859	87,802
Others liabilities	42,175	41,456	43,032	37,839	45,409	46,415
Shareholders' funds	50,365	49,972	42,137	43,032	86,502	90,376
Total Liabilities	141,666	142,550	134,635	131,763	223,770	224,594
Capital employed	100,964	113,052	108,373	104,434	149,108	192,561
Financial Ratios						
Operating margin	32.88	32.53	31.58	31.51	34.13	35.50
Tax rate	11.05	18.12	20.82	22.00	22.00	23.00
Net margin	18.37	18.84	19.52	17.50	19.08	20.06
ROE (after tax)	15.76	17.74	20.20	17.50	12.86	13.51
ROCE (after tax)	12.51	11.09	10.06	10.13	10.41	8.64
Gearing	15.76	83.48	98.68	102	97.05	89.48
Pay out ratio	44.13	49.58	52.50	52.50	52.50	52.50
Number of shares, diluted	1,650	1,665	1,668	1,668	1,994	1,994
Data per Share (USD)						
EPS	8.72	5.54	4.96	3.58	5.55	6.10
Restated EPS	4.81	5.32	5.10	4.52	5.58	6.12
% change	*8.7%*	*10.7%*	*-4.1%*	*-11.5%*	*23.5%*	*9.8%*
BVPS	31.32	31.08	26.20	26.76	44.73	46.73
Operating cash flows	10.05	10.73	9.76	9.98	13.21	12.88
FCF	8.45	5.64	4.63	3.90	6.96	6.33
Net dividend	2.12	2.64	2.68	2.37	2.93	3.21

Source: Company Data; Bryan, Garnier & Co ests.

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1. Executive summary

1.1. Target USD100bn

2020 Dream Incentive Plan encourages AB InBev's top management to come up with new external growth options: PepsiCo and The Coca-Cola Company would fit

In December 2015 (so after the SABMiller deal was agreed), AB InBev set up its "2020 Dream Incentive Plan", which incentivises the top 65 managers to bring in to the company a turnover of USD100bn by 2022 at the latest. As, by then (2022), AB InBev's revenues (after the SABMiller deal) would reach, according to our forecasts, just over USD70bn, the company will be USD30bn short of its target. With opportunities in beer being limited, given the size of the company in most markets and the similarity between beer and soft drinks in producing, distribution and selling, our current view is that there are only two external growth opportunities that generate about USD30bn in revenues: The Coca-Cola Company post refranchising (USD30.0bn in 2020e) and the beverages business of PepsiCo (USD33.9bn in 2020e).

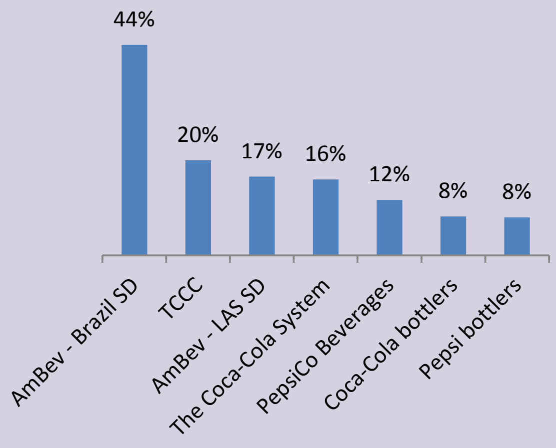
PepsiCo's acquisition could be quickly 50% EPS enhancing

There are plenty of reasons why PepsiCo would fit in well: a combination would create a global brand power house; in the US it is already buying up certain items like media and travel; AB InBev already bottles, distributes, sells PepsiCo products in Brazil; there is a similar vision of creating a better world; PepsiCo's beverages have an addressable cost base of USD29bn across production, distribution and sales. Furthermore, AB InBev could move together with Kraft Heinz which might be interested in the Snacks business (64% of EBIT) and AB InBev in the beverages business (36% of EBIT). For AB InBev, this would allow a manageable bill of USD100bn, which could be entirely debt-financed. Assuming that AB InBev can combine PepsiCo's beverages with its beer production, distribution and sales, efficiency savings could well be up to 20% of acquired revenue (USD5.9bn), enhancing AB InBev's EPS by 40%. However, PepsiCo's beverage business is a global number two and, from experience in Brazil, AB InBev knows that outgrowing Coca Cola is extremely difficult, if not impossible. Also, after a PepsiCo deal, AB InBev would find it more difficult to find further external growth opportunities.

The Coca-Cola Company acquisition is likely to be only 20% EPS enhancing but with options to buy out bottlers as time goes by, a deal could improve EPS by 90%.

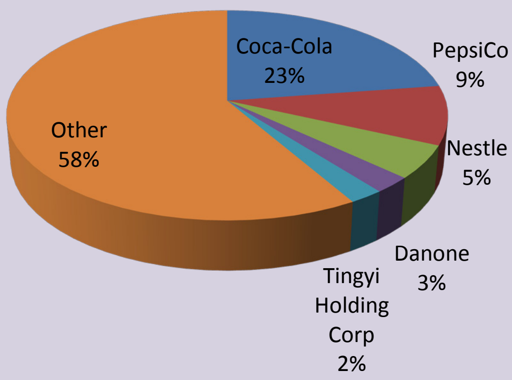
We believe that The Coca-Cola Company (TCCC) would be a more attractive target. In the short term, it is a more difficult acquisition (USD300bn, of which 55% needs to be financed in equity), the earnings enhancement is not as big (+20% on EPS) because there will be 50% more AB InBev shares and the addressable cost base is limited (USD20bn). However, revenue growth is likely to be faster, at 6.5%, compared to 4% at PepsiCo and TCCC would be only a first step. After integrating TCCC and paying down debt, AB InBev would be able to start consolidating the Coca-Cola bottlers, which in the end control access to the customer. Indeed, converse to PepsiCo, which is strongly vertically-integrated, TCCC works with a franchise model. Buying out the Coca-Cola bottlers (which would be debt-financed) would enhance revenues by another USD70bn and allow access to USD13bn of additional savings. So, a full acquisition of the Coca Cola system, spread out over 10 years, or so, would enhance EPS by 90% (organic growth at AB InBev and the Coca-Cola system would come on top)! Coupled with organic growth, the result would be an AB InBev company doing USD300bn of revenues in 2030. Furthermore, there are external growth opportunities in non-alcoholic beverages that AB InBev would be able to take. Buying out the bottlers is not necessarily going to be expensive as TCCC can set prices unilaterally for its concentrate, diminish marketing support and can force owners to sell. An interesting case will be Coca-Cola Beverages Africa in which AB InBev would hold 57%. For the moment, there are strong indications that TCCC plans to buy back this stake and sell it on to Coca Cola Hellenic which would be asked to sell its Western Europe operations to Coca Cola European Partners. It might highlight that bottlers are not worth much more than their net asset value as they live by the grace of TCCC. Acquiring TCCC would need significant skills, navigating the minefield of politics. We believe that the Belgo-US-Brazilian combination with the HQ in New York and strong US allies (AB, Altria, Buffett, Santo Domingo) and links with the ownership of strong US names, such as Burger King and Kraft Heinz, has exactly those credentials to pull it off.

Fig. 1: AB InBev has great capabilities in managing soft drinks (operating margins 2015)



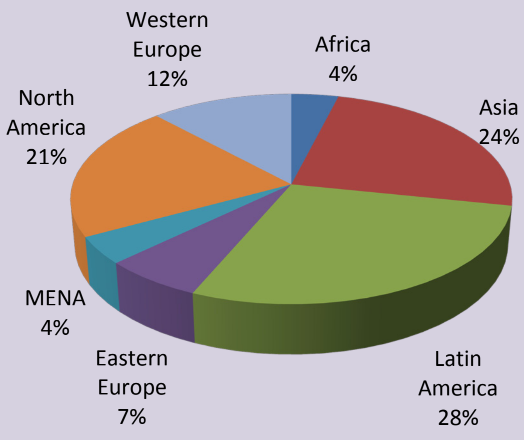
Source: Companies, Bryan, Garnier & Co ests

Fig. 2: The global non-alcoholic drinks market (in volume, 2015)



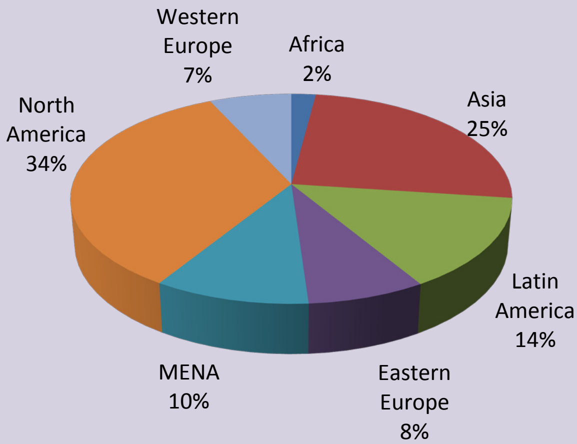
Source: Canadean

Fig. 3: Coca-Cola system wide sales volumes by region (144m hl, 2015)



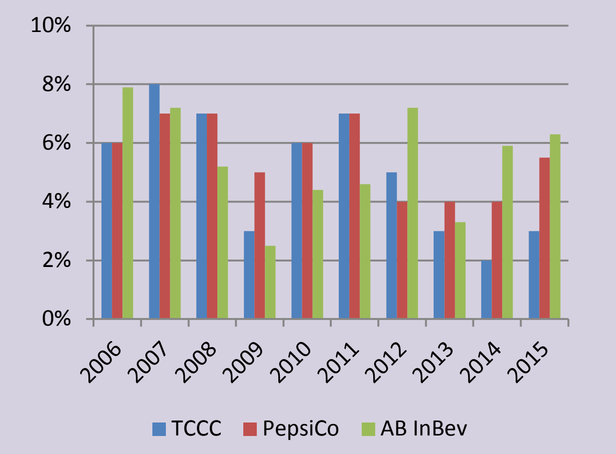
Source: Canadean

Fig. 4: Pepsi system wide sales volume by region (58m hl, 2015)



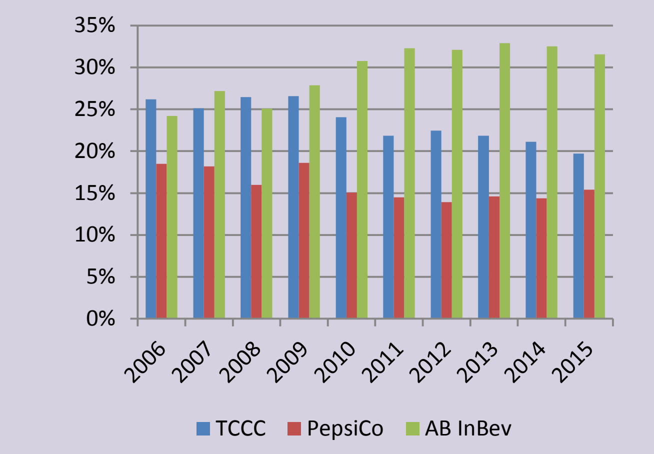
Source: Canadean

Fig. 5: Organic revenue growth compared



Source: Bryan, Garnier & Co ests

Fig. 6: Operating margins compared



Source: Bryan, Garnier & Co ests

1.2. The attractiveness of investing in AB InBev

1.2.1. Successful serial acquirer

Already the early signs were about dramatically cutting costs and improving profits

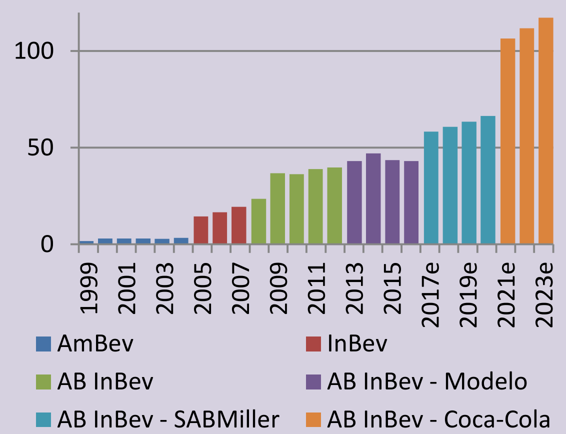
Back in 1989, Marcel Telles (also one of the founding partners of 3G Capital together with Jorge Paulo Lemann, Carlos Alberto Sicupira, Roberto Thompson, and Alex Behring), joined Brahma and turned the largest brewer in Brazil into a lean operation, cutting employee numbers by two and raising EBITDA to USD505m in 1999 (from USD60m in 1989 = x8) on revenues of USD1.8bn. In July 1999, Brahma merged with the second largest Brazilian brewer Antartica, naming the new company AmBev. The deal gave it 70% of the Brazilian beer market and, in 2000, the company was the third largest brewer in volumes in the world, behind Anheuser-Bush and Heineken. From revenues of USD3.0bn in 2000, the company grew organically to USD3.4bn in 2004, whereas operating profits doubled to USD1.0bn in that period. A reverse take-over with Interbrew from Belgium, created InBev, which became the world's largest brewer with a 14% share, ahead of Anheuser-Busch and SABMiller. The acquisition of Anheuser-Bush in 2008, Modelo in 2013 and SABMiller in 2016, continually expanded its global lead. And with each acquisition the same scenario was repeated: drastic and quick cutting of costs to enhance the group's overall operating margin. Revenues of the original AmBev should grow to USD58.3bn in 2017e (first year of full consolidation of SABMiller) from USD3.0bn in 2000 (that is x19!!, with acquisitions). The operating margin continued to expand from 18% in 2000 to an estimated 34.1% in 2017 and operating profit will grow to an estimated USD19.9bn from USD525m in 2000 (x38!!).

Since 2000, controlled revenue x19 and operating profit x38

And it is not going to stop there, TCCC could well be the next one

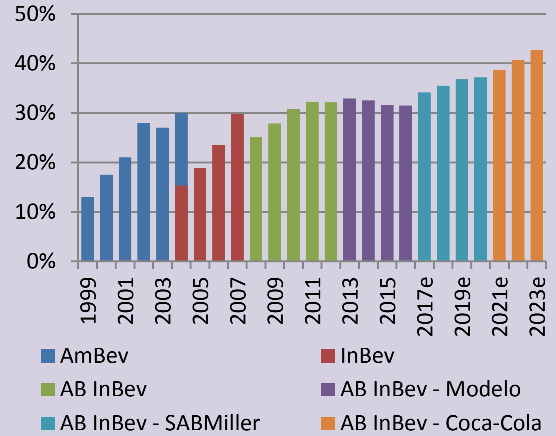
We believe that the company will not stop expanding and will look for further acquisitions in both beer and adjacent categories like soft drinks (after all, soft drinks has been part of their business since 2000). One possible scenario is that AB InBev buys TCCC and afterwards buys out gradually the bottlers as and when they become available. This could propel the company to a USD300bn revenue company by 2030.

Fig. 7: Acquisitions propelling Ambev from a Brazilian brewer to the largest global consumer goods company



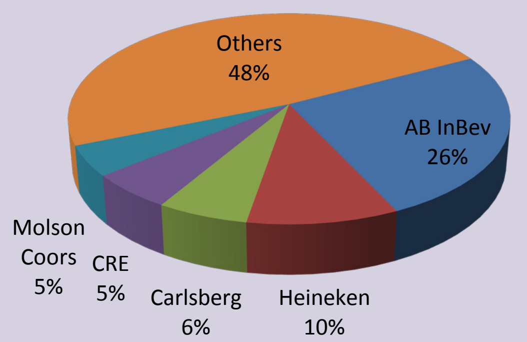
Source: Companies, Bryan, Garnier & Co ests

Fig. 8: Acquisitions as opportunities to improve operating profit margin



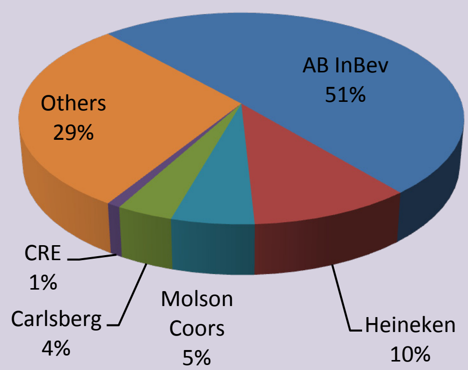
Source: Companies, Bryan, Garnier & Co ests

Fig. 9: Global beer market share volume, 2017e



Source: Canadean

Fig. 10: Global beer market profit pool, 2017e



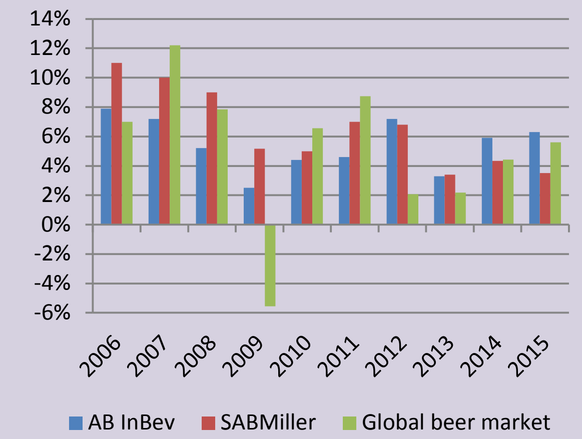
Source: Bryan, Garnier & Co ests

1.2.2. Strong organic growth profile

Growing revenues ahead of the global beer market

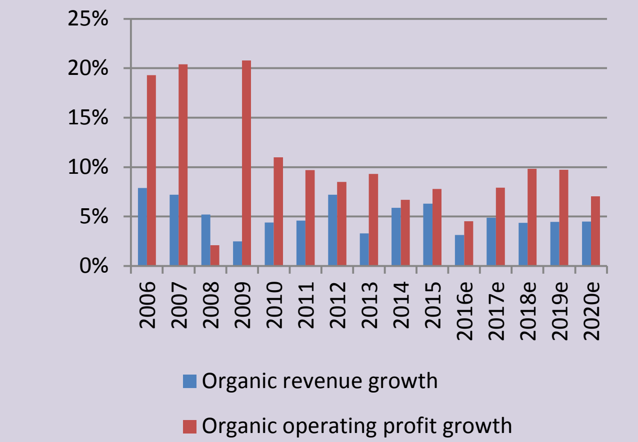
AB InBev is growing revenue ahead of the global market. During the past ten years, organic growth of the global beer market has been 4.9% in USD and 2.7% in volumes. AB InBev has been doing slightly better with 5.5% organic revenue growth, and SABMiller's has been 6.5% given its exposure to the developing markets. Both AB InBev's and SABMiller's absence in the European market explain their much better performance in 2009, but even excluding the weaker European market in 2009 and its rebound in 2010, both companies have been doing better than the global beer market.

Fig. 11: Organic revenue growth ahead of the global beer market



Source: Bryan, Garnier & Co ests

Fig. 12: Delivering organic operating profit growth ahead of organic revenue



Source: Bryan, Garnier & Co ests

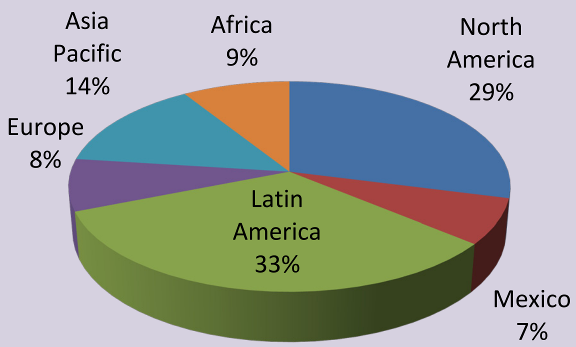
And growing operating profit ahead of revenues, 11.6% vs. 5.5% in the past ten years

Furthermore, AB InBev's attention to cost (zero-based budgeting, plant optimisation) and the inclusion of newly-acquired companies in the same philosophy, has enabled it to deliver continually better organic operating profit growth (11.6% on average over the past ten years) than revenue growth (5.5%). We believe this trend will continue and look for, in the next five years, an average of 7.8% organic operating profit growth on 4.3% organic revenue growth. Drivers for both top-line and profit growth would include:

Emerging market exposure: Volume growth tends to be faster in emerging markets as the economies develop and consumers up-trade to beer. We estimate that after the SABMiller acquisition, developing markets will be 63% of 2015pf revenue compared to 53% for AB InBev previously.

Premiumisation: Over the past decade, premium beer has grown volumes by 3.8% p.a. and super premium beer by 4.8% p.a. compared to 2.5% growth in mainstream. AB InBev is well placed to play on this trend given its high exposure to Africa and Latin America, where consumers trade up from the informal/home-brew market (still 75% in Africa and 25% in LatAm). But also high-end beer is only 15% of volumes in Africa and Latin America and 10% in Asia compared to 30% in Australasia, North America and Europe. And, although the international premium Budweiser accounts for only 3% of the company's volumes, the potential to develop the brand globally is there (and the proof is there that the company has been able to do this in Brazil and Mexico). Furthermore, AB InBev has come to the conclusion that it was missing the entire craft brew development in the US and has now made a series of acquisitions in craft brew to correct its US position, but has also gone further and acquired craft brewers in Brazil, Colombia, Mexico and the UK. – determined not to miss the boat again.

Fig. 13: AB InBev revenue split post SABMiller



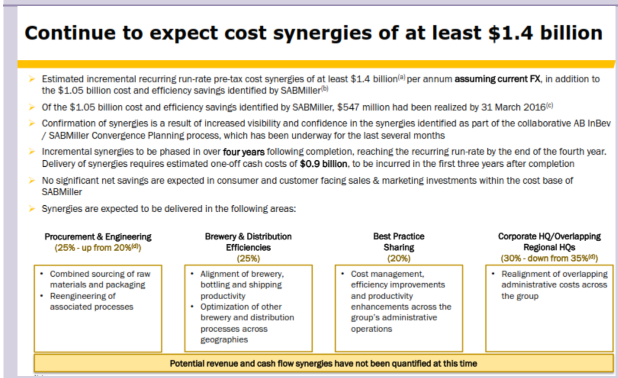
Source: AB InBev

Fig. 14: Penetration high-end beers by region

Source: Canadean, Bryan, Garnier & Co ests

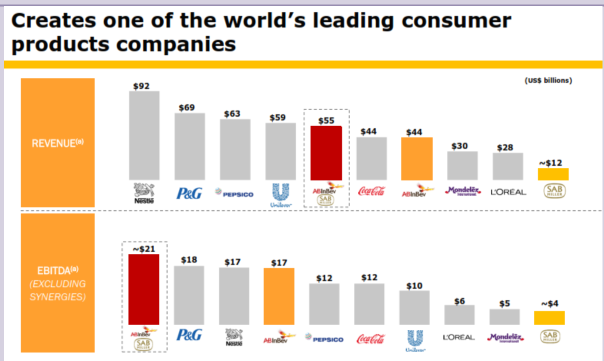
Efficiency improvements: AB InBev believes that it can save at least an additional USD2bn (of which USD650m remaining from a USD1.05bn cost savings plan from SABMiller and an incremental USD1.4bn), which is 17% of the net revenue of the SABMiller activities that are not divested. We believe that the company will be able to save USD3bn, i.e. 25% of revenues.

Fig. 15: AB InBev expects at least USD1.4bn extra savings



Source: AB InBev

Fig. 16: Penetration high-end beers by region



Source: AB InBev

2. Setting the scene: the 2020 Dream Incentive Plan

Internal target to achieve USD100bn of revenue by 2022…

On 18th December 2015, AB InBev published its "2020 Dream Incentive Plan", which awards 6m options on AB InBev shares (we estimate an exercise price of USD115 which was the share price on that date) to the top 65 managers and which are conditional upon AB InBev reaching net revenue of at least USD100bn in 2020, 2021 or 2022. Although the 16 top managers, who are on the executive management board, are excluded from the programme, we deduce from the CEO Brito's comments during the call on the Q1 2016 results that a similar, non-public, target exists for the managers on the executive management board, including himself and the CFO, as we believe that theirs and the top 65 managers' bonus plans (CEO and CFO) are strictly aligned to internal targets. Brito said "We decided to link it (the 2020 Dream Incentive Plan) to a target that we have internally. This is not company guidance or anything, in terms of 2020 or anything. We have all sorts of targets and dreams that we have for different business units, for different lines of the P&L inside the company. And from time-to-time, we connect some of those incentives to some of those dreams." In our view, the company would not link such an important and long-term incentive to something which is uncertain and unlikely to happen. Again Brito "…. we always put targets and dreams via yearly or multiyear (plans) in which we know 70%, 80% how to get there. And we feel that that's the way to build the company, because then it gets people to be creative. It gets people to use their best part of their brain to try to bridge gaps, and that's how we've always managed the company – that the one we mentioned is just one more example of that stretched target".

…organic or through acquisitions

To reach the USD100bn revenue by 2022, the plan leaves open the possibility to achieve it through organic or external growth or a combination. To do so organically, AB InBev should, starting next year, grow its revenue organic by 12% p.a. for five years. This seems a hard task given that over the past 10 years AB InBev's organic revenue growth was 5% p.a. even though at SABMiller it was 7% p.a. Hence, the speculation is about what else could be of interest to the company to achieve this "internal stretch target". And because there is a belief that AB InBev is now the complete global brewer, and hence further brewer acquisitions could only be limited, speculation has turned around a potential combination with the soft drinks giants The Coca-Cola Company and PepsiCo.

Combining beer with soft drinks could make sense

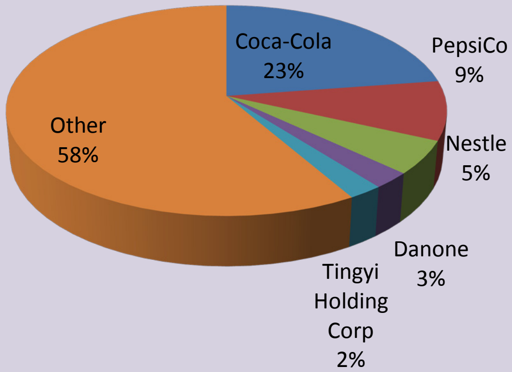
Combining beer with soft drinks could make sense. Indeed, there are emerging markets where beer and soft drinks are distributed together (especially in the early stages of development of these markets), but sometimes brewers have been divesting their soft drinks business in order to run two different distribution platforms when these businesses became more mature. This was the case with SABMiller in Colombia but also the creation of Coca-Cola Beverages Africa fits the same idea. Femsa went the other way, divesting its beer business to Heineken in exchange for an equity stake.

However, in some more mature emerging markets, beer and soft drinks are still held by the same company. In Brazil, Heineken's products are sold through Coca-Cola bottlers. But also in mature markets, there are integrated beer and soft drinks operations. SABMiller bottles Pepsi in Panama. Carlsberg has fully integrated beer and CSD operations in the Nordics: in Denmark and Finland, the company distributes Coca-Cola, and in Norway and Sweden, Pepsi. Pepsi is also integrated with Royal Unibrew's beer operations in Denmark, Finland and the Baltic countries. Asahi and Kirin hold both soft drinks and beer/spirits operations.

AmBev has successfully fully integrated soft drinks with beer in Latin America

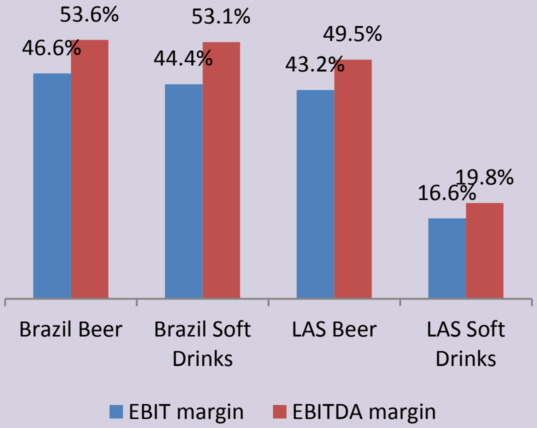
However, the most interesting example is Ambev (AB InBev's Brazilian subsidiary) that has fully integrated its beer and CSD operations in most of South America. In Brazil, AmBev produces, distributes and sells soft drinks (1/3rd PepsiCo's products, 2/3rds own brands) together with beer. As a result, its 2015 operating margin in soft drinks in Brazil was 44.4%, close to the operating margins for its Brazilian beer business of 46.6%. In the Latin American South business, soft drinks are also distributed with beer, but here AmBev only sells PepsiCo's products, the result is much smaller EBIT margins at 16.6%, which is still 10% ahead of what similar bottling operations can achieve.

Fig. 17: Global soft drink market in volume, 2015



Source: Canadean

Fig. 18: Ambev's Brazilian and Latin America South soft drinks and beer margins



Source: AmBev

What would fit best: The Coca-Cola Company or PepsiCo?

So the big question is what would fit best within AB InBev: The Coca-Cola Company or PepsiCo. There are arguments for both scenarios. TCCC's's CEO Kent has already warned his management that 3G Capital Partners (controlling shareholders of AB InBev) could try to acquire the company (3G co-investor Warren Buffet already is the largest Coke shareholder). And the newly-acquired SABMiller is already bottling Coca-Cola in numerous markets in Southern Africa and Central America (Honduras and El Salvador). On the other hand, AB InBev has long-standing relationships with PepsiCo (including a common buying platform in the US and being their bottler in Brazil, Argentina, Bolivia, Uruguay, Peru and the Dominican Republic). Furthermore, PepsiCo's revenues of USD63bn are USD31bn beverages and USD32bn snacks which could facilitate a joint offer from AB InBev and Kraft Heinz (also controlled by 3G Capital Partners).

3. The Coke Option

The Coca-Cola Company (TCCC) would be an attractive asset for AB InBev with significant opportunities to cut costs. Not only does it own iconic brands, it also provides significant growth opportunities (in sparkling and still) and opportunities to improve profitability. Following on from the comments made by the company's CEO Kent, the company has embarked on a significant restructuring plan which includes divesting its North American bottling operations and an efficiency plan. Adjusting the company's 2015 earnings for the bottler transactions, the remaining business would have generated in 2015 pro-forma revenues of USD28.5bn and an operating profit of USD9.5bn. From the adjusted spend base of USD19bn, the company's own plans are already looking to cut this by USD3bn (16%), of which 1/3rd would go to operating margin expansion.

USD5.9bn synergies for TCCC under AB InBev …

However, we believe that AB InBev could save another USD5.9bn including the USD1.1bn of corporate costs (finance, management, IR, legal, HR, etc.). Unlike what is happening with the cost savings that TCCC is making, these savings would be able to go towards an increase in the operating margin to 57% (from 37% under TCCC's own plans). We wonder if TCCC, with its zero-based work, could also up its savings targets further in the direction of USD5.0bn (instead the USD3.0bn). Furthermore, there should be numerous opportunities to reintegrate the bottling system worldwide, which should provide AB InBev a continuous stream of integration synergies. After all, its fully-integrated Brazilian soft drinks and beer business does provide for similar operating margins (44.4% and 46.6% respectively).

… and another USD13bn through integrating bottlers

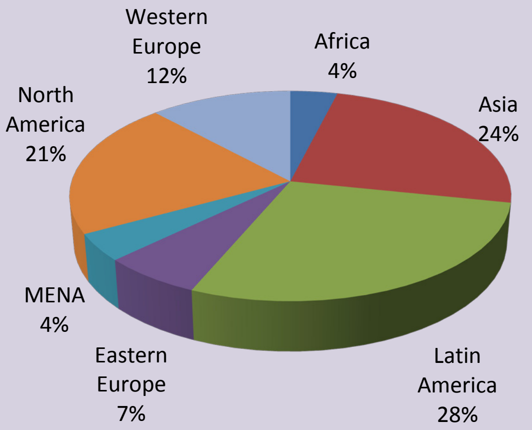
On the basis of USD99.3bn of system-wide sales, the Coca-Cola system is earning today USD15.4bn, that is an operating margin of 16% (all Bryan Garnier's estimates). If AB InBev manages over time to generate a 35% operating margin on this, it would tap into USD18.9bn of synergies, of which USD5.9bn for TCCC and USD13.0bn from the bottlers.

3.1. The Coca-Cola Company as brand owner

TCCC has a 23% global market share, well ahead of PepsiCo's 9%

Founded in 1886, TCCC is the world's largest non-alcoholic drinks company and is active in more than 200 countries. It controls a 23% volume share in global non-alcoholic ready-to-drinks, which is well ahead of the 9% from PepsiCo. The Coca-Cola system sold 165.8bn litres of products in 2015, of which 73% in the sparkling segment and 27% in the still segment. According to Canadean, Latin America is the largest region for its products, accounting for 29% of volumes, followed by Asia (24%) and North America (21%).

Fig. 19: Coca-Cola system-wide sales volumes by region (144m hl)



Source: Canadean

Fig. 20: Some TCCC main brands and year of introduction

Brand	Year introduced	Segment
Schweppes (outside US)	1783	Sparkling
Coca-Cola	1886	Sparkling
Fanta	1940	Sparkling
Minute Maid	1945	Still
Del Valle	1947	Still
Sprite	1961	Sparkling
Georgia Coffee	1975	Still
Diet Coke/ Coca-Cola Light	1982	Sparkling
Aquarius	1982	Still
Powerade	1988	Still
Bunaqua/Bonaqa	1988	Still
Glaceau Smartwater	1996	Still
Dasani	1999	Still
Glaceau Vitaminwater	2000	Still
Simply	2001	Still
Coca-Cola Zero	2005	Sparkling
Minute Maid Pulpy	2005	Still
Gold Peak	2006	Still
Ayataka	2007	Still
Fuze Tea	2012	Still
I Lohas	2012	Still
Ice Dew	2014	Still

Source: Canadean

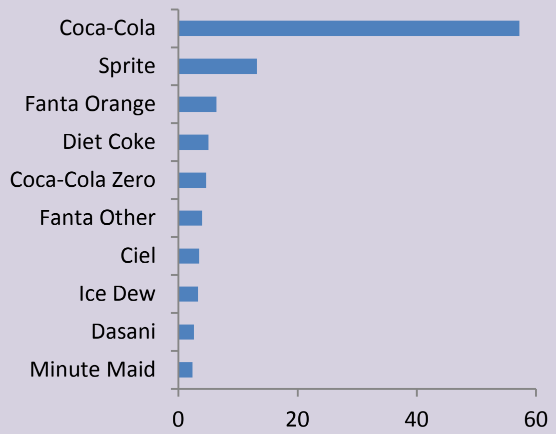
It owns 5 of the top 10 non-alcoholic RTDs: Coca-Cola, Diet Coke, Sprite, Fanta and Mountain Dew

Its brands include five of the world's top ten non-alcoholic ready-to-drinks (RTDs): Coca-Cola, Coca-Cola Light (Diet Coke), Sprite, Fanta and Mountain Dew. In total, the company has 20 one-billion dollar brands and a strong pipeline of growing regional brands across sparkling packaged water, juice, juice drinks, energy drinks, ready-to-drink tea and dairy.

TCCC is responsible for consumer marketing, brand development and making the concentrate. The bottlers distribute and sell in local markets

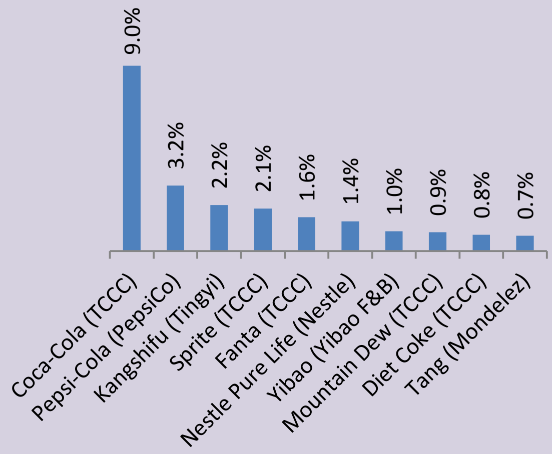
TCCC and its 250 bottling partners together make up the Coca-Cola system where TCCC is responsible for creating demand through consumer marketing and brand development. It also sources ingredients and manufactures and sells concentrates, drinks bases and syrups to bottling operations. The bottling partners (not all are owned or controlled by TCCC) combine the insights, resources and experience of TCCC with their own expertise in bottling, distribution and sales. The bottling partners are responsible for meeting demand through manufacturing, packaging, distributing and merchandising the finished branded soft drinks to customers – grocery stores, restaurants, convenience stores, cinemas, theatres and amusement parks, among many others, which then sell on the products to consumers. They are also responsible for customer marketing and outlet execution.

Fig. 21: TCCC main brands – global sales volumes, 2015



Source: Canadean

Fig. 22: Global top 10 non-alcoholic beverages, 2015



Source: Canadean

3.2. How does Coke make money?

Selling concentrate to bottlers

TCCC has two businesses. The first one is the concentrates business where the company generates revenues by selling concentrates and syrups (including fountain syrups) to authorised bottling partners. These bottling partners either combine the concentrates with sweeteners (depending on the product), still water and/or sparkling water, or combine the syrups with sparkling water to produce the finished beverages. The finished beverages are packaged in cans, refillable and non-refillable glass, and plastic bottles. They are then sold to retailers directly or, in some cases, through wholesalers.

Selling finished products like juice, energy drinks, sport drinks, water, etc., to distributors, wholesalers and bottling partners

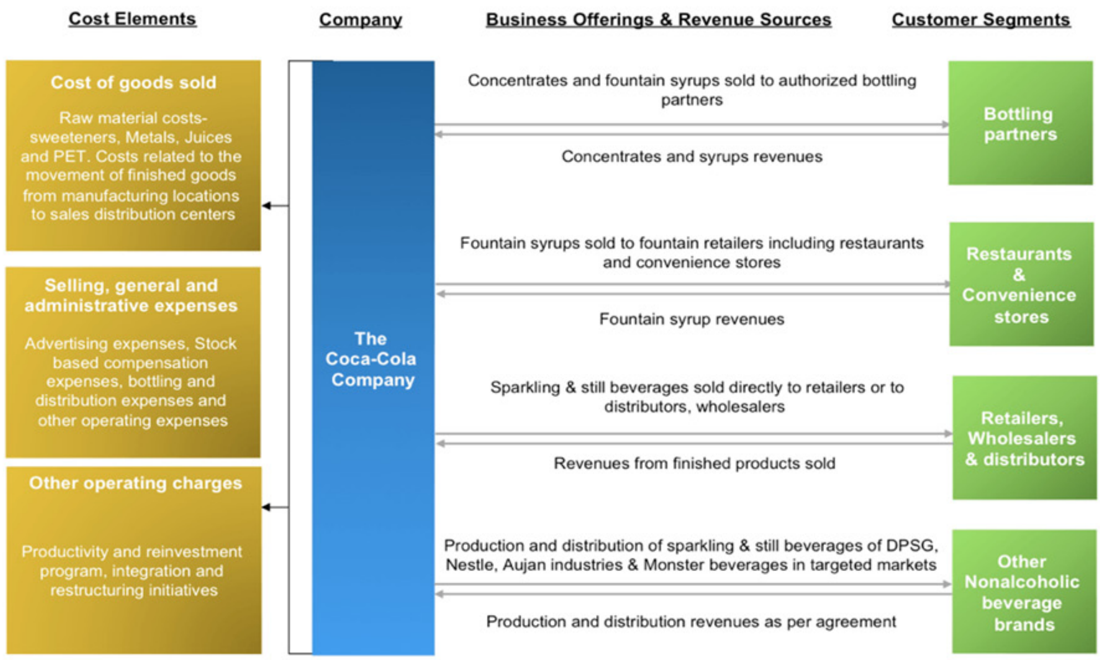
The second business of TCCC is the finished products. In this, the company generates revenues by selling sparkling beverages and a variety of still beverages, such as juices and juice drinks, energy and sports drinks, ready-to-drink teas and coffees, and certain water products, to retailers or to distributors, wholesalers and bottling partners which distribute them to retailers. In addition, the company manufactures fountain syrups and sells them to fountain retailers, such as restaurants and convenience stores which use the fountain syrups to produce beverages for immediate consumption. Outside the United States, it sells concentrates for fountain beverages to the bottling partners that are authorised to manufacture fountain syrups, which they sell to fountain retailers or to authorised fountain wholesalers which in turn sell and distribute the fountain syrups to fountain retailers.

The company also gets revenues by providing marketing support and selling other non-alcoholic beverage brands that include DPSG, Nestle, Aujan industries and Monster beverages through licences, joint ventures and strategic partnerships. The company has also entered into the at-home dispensing market by its partnership with Keurig for the production and sale of its branded single-serve, pod-based cold beverages.

Long contracts but TCCC has plenty of leavers to influence bottlers' margins and shareholding structure

The length of the contracts with bottlers varies, but the new ones tend to be 25 years. However, there are plenty of options for TCCC to force the bottler to comply. We understand that, for instance, contracts can be broken if products are not on the shelves and also TCCC has complete freedom in pricing its concentrate product (but will take into account the competitive situation). Originally, it was pricing its products at a fixed price, which created a focus on volume, but increasingly the company changed pricing to the "incidence" approach, whereby both TCCC and the bottler share in the profit made by the combined system, rather than a fixed price per unit for concentrate. This approach allows for a focus on value rather than volume growth (for instance, selling small bottlers in coolers at service stations compared to selling 2 litre PET bottles).

Fig. 23: How does TCCC make money?



Source: www.revenuesandprofit.com

3.3. Where is the company going?

At the end of 2014, TCCC's Chairman and CEO Ahmet Muhtar Kent, laid out a five-point agenda:

3.3.1. Streamlining and simplifying TCCC's operating model

TCCC focuses on the back-office and production, bottlers in local markets, distribution and sales

TCCC is streamlining and simplifying its operating model in order to speed up decision-making and enhance its local market focus to drive growth. There are various aspects to this strategy. TCCC will focus on those roles where scale is important (manufacturing, IT and shared services) and the bottlers can focus on growth and demand creation in their individual markets. The result should be a more nimble organisation that can act more rapidly and an enhanced local market focus.

3.3.2. Expanding its productivity programme from an original USD1bn to USD3bn

In February 2014, TCCC announced that it was planning to save an additional USD1bn by 2016 – the majority of which would be reinvested in marketing to restore the company's growth. The turnaround plan covered five areas (which have not changed since then): accelerating growth of its sparkling portfolio, strategically expanding the profitable still portfolio, increasing media investments by maximising systems optimisation, making improvements to point of sale and investing in the next generation of leaders.

Saving USD3bn in the 2014-2019 period

However, in October 2014, the company announced an incremental USD2bn savings by 2019. These additional productivity initiatives focused on four key areas: 1) restructuring the company's global supply chain, including manufacturing in North America; 2) implementing zero-based work (zero-based budget principles but also taking into account what is non-value-added work), across the organisation; 3) streamlining and simplifying the company's operating model; and 4) and further driving increased discipline and efficiency in direct marketing investments.

By the end of 2016, USD1.8bn will be done

At the end of 2016, the company will be just over half way to realise these savings (USD1.8bn). From the cost base that is left in the company after the refranchising, i.e. USD19bn (2015 figure), the aim is to save USD3bn (16% of the spend base) or USD0.5bn p.a. USD1.1bn savings are expected to come from COGS (12%) and USD1.9bn from SG&A (19%). COGS include raw material costs (sweeteners, metals, juices and PET) and costs related to the movement of finished goods from manufacturing locations to sales distribution centres. Operating expenses include: a) SG&A (selling, general and administrative expenses) including advertising expenses, stock-based compensation expenses, bottling and distribution expenses and marketing expenses like in-store activations, loyalty points programmes and point-of-sale marketing, and b) other operating expenses (productivity and reinvestment programme, integration and restructuring initiatives).

USD3bn is 16% of the company's cost base

Fig. 24: Productivity targets represent a sizeable reduction of spend

USD, 2015 pf	COGS	SG&A		Total
Adjusted spend base	USD9bn	USD10bn		USD19bn
		Opex	**Marketing**	
Total savings	USD1.1bn	USD1.2bn	USD0.7bn	USD3bn
Percentage of spend base	12%	19%		16%

Source: Coca-Cola

About half of the original USD3bn savings was expected to come from the supply chain and, because of the size of the US market, a significant portion should come from the US. However, because of the refranchising, a portion of these supply-chain savings could no longer be captured. As a consequence, the company identified additional cost savings opportunities in cost of goods sold, operating expenses and marketing to repay for the supply-chain savings being refranchised, thus maintaining the USD3bn target. The ease at which the company identified additional savings could indicate that the potential is higher than the stated USD3bn (we believe that AB InBev could increase savings to USD6bn).

Bottlers working together in purchasing

What is more is that the "lost" USD500m will be captured by the US franchise system and TCCC has already indicated that it hopes it (the franchise system) can find additional areas to increase this. (Because of the new incidence model, where TCCC is paid as a percentage of gross profits, TCCC has some stake in that as well.) Furthermore, most of the bottlers are in the cross enterprise procurement group to purchase some key commodities together like IT, aluminium, bottles, caps, etc.), but additional ideas are emerging as bottlers extend their territories (for instance, CCEP can now also tap into Coca-Cola Germany's knowledge on how to deal with discounters and into Coca-Cola UK's and Spain's knowledge on dealing with the horeca).

3.3.3. Refocusing on its core business model

Refranchising all its bottling operations

With refocusing on its core business of building brands and leading its system of bottling partners, the company is aiming to become "lower risk and higher return". To a large extent this refocus is about refranchising bottling activities, not only in North America but also of company-owned or -controlled bottling operations in Europe, Africa, China and Japan.

In the US, the company has already refranchised 70% of its volume and is still on track to complete the refranchising by the end of 2017. With the creation of Coca-Cola European Partners and Coca-Cola Beverages Africa, the company *de facto* refranchised, respectively, its European and African operations. In China, the company is in the process of refranchising its bottling operations to its existing partners COFCO and Swire. In Japan, the company is eyeing up a potential merger of the East (30% owned) and West (4% owned) bottling operations.

What is left is a USD28.5bn turnover company making a USD9.6bn operating profit (2015 pro forma)

Once all this refranchising is completed TCCC will look very different. Only 3% of global bottling volume will be done by the company (concentrated in Asian countries and India) compared to 18% in 2015 and the number of employees will fall to 39,000 (of which half will be in the remaining bottling territories) from 123,000. Post refranchising, the company is expected to record net revenues of USD28.5bn, an operating margin of 34% and a free cash flow margin of 27%. However, these figures are based on 2015 numbers and do not include further growth in the Coca-Cola system, cost savings, the quarterly profit share from the divested US operations. Furthermore, the company would also receive its profit share from the equity ownership in bottlers, including 28% in Coca-Cola FEMSA, 24% in Coca-Cola Hellenic and 20% in Coca-Cola Içecek, 29% in Coca-Cola Amatil 18% in Coca-Cola European Partners, 11.3% Coca-Cola Beverages Africa, 16% Coca-Cola Japan.

Fig. 25: Simplified P&L of TCCC, pre and post refranchising

USD bn	2015	2015PF post
Net revenue	44.3	28.5
Gross margin	61%	68%
Operating income	10.4	9.6
Operating margin	23%	34%
Capex	2.6	1.3
Free cash flow	8.0	7.6
FCF margin	18%	27%

Source: TCCC; Bryan, Garnier & Co ests

3.3.4. Targeting disciplined brand and growth investments

2/3rds of savings to be reinvested in marketing and innovation

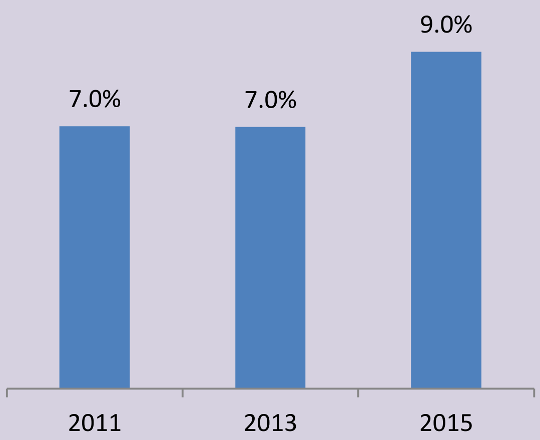
We understand the majority of the USD3bn efficiency programme (USD0.5bn p.a.) that was launched in 2014 will be used to fund marketing initiatives and innovation (2/3rds) to drive net revenue growth and the smaller part (1/3rd) to support margin expansion and increased returns on invested capital over time.

As a result, TCCC has been increasing its media investments in markets and categories where it feels it was underfunded relative to the market opportunity, where it has the right price/package architecture and where it has a clear executional alignment with its bottlers. Indeed, advertising expenses increased by 7% in 2014 and 14% in 2015 and, as a percentage of net revenue, went from 7% in 2013 to 9% in 2015. In absolute numbers, the company spent in 2014 an additional USD228m (USD3.5bn) and in 2015 USD482m (USD4.0bn). According to the company, the 4% price/mix increase in North America in the second half of 2015 indicated the initial success of the strategy.

The Coca-Cola system spend is well ahead of what PepsiCo is spending to promote its brands

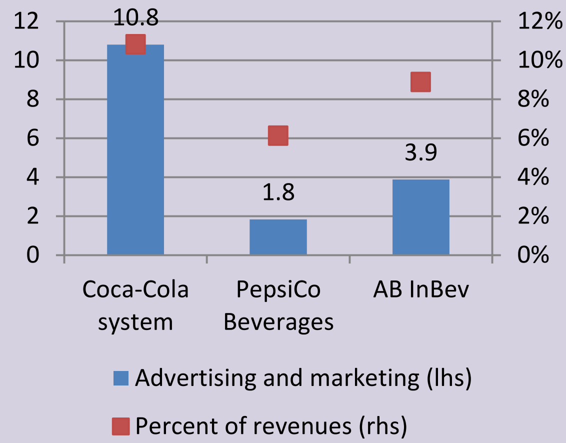
Next to advertising investments, the company also provides promotional and marketing services and/or funds to its bottlers. But these amounts have been flattish over the past three years as the company spend was USD6.9bn, USD7.0bn and USD6.8bn in 2013, 2014 and 2015 respectively. However, we believe that both have to be looked together. The direct USD4.0bn advertising and marketing spend from TCCC is used to over the medium and long term, develop the brand image and pull consumer demand. The bottler support is actually TCCC taking on board, as we understand it, all advertising and marketing to develop short-term demand. For this spend, it would be TCCC and the bottler deciding together on what and how to spend it, but it would be TCCC that pays the bill. So the overall Coca-Cola system spend is about USD10.8bn or 11% of system wide sales. This compares with USD1.8bn at PepsiCo (for the beverages division alone), immediately indicating why PepsiCo will continue to find it difficult to fight TCCC. These figures compare with brewers which tend to spend 9-11% on marketing, with AB InBev spending about 9% of revenues (pre-SABMiller) or USD3.9bn.

Fig. 26: TCCC direct advertising and marketing spend as a % of revenues



Source: TCCC

Fig. 27: Advertising and marketing spend compared (USDbn, rhs) and % of revenues (lhs)

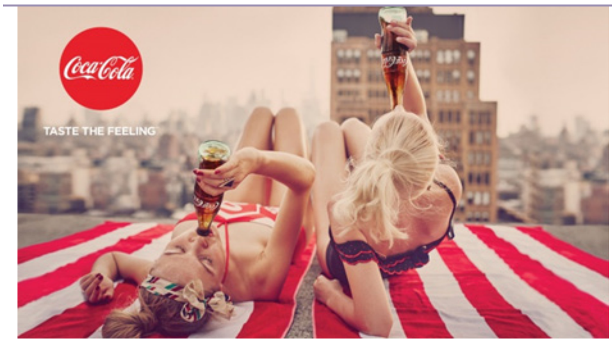


Source: Bryan, Garnier & Co ests

One brand look

Next to the reinvestment strategy, the company is reformulating a one brand strategy that brings back under one umbrella the different Coke brands, Coke, Coke Zero, Diet Coke, Coke Light, Coke Caffeine-Free, Coke Life, Cherry Coke, Vanilla Coke, etc. The company has been linking the Taste the Feeling campaign to marketing Coca-Cola as One Brand with a number of product variants rather than lots of separate brands. Incidentally, this approach also allows reducing the number of agencies leveraging production costs.

Fig. 28: Taste the Feeling



Source: TCCC

Fig. 29: One Brand look

Source: TCCC

3.3.5. Driving revenue and profit growth with clear portfolio roles across its markets

TCCC segmented its markets to develop long-term revenue growth strategies based on volume, price, investment and profit expectations. This means that some markets focus on price growth, others on volume and some on both.

3.4. Expected to grow top-line at 6.5% p.a.

Company is guiding for 5% annual top-line growth (4% in 2016 and 2017)

According to TCCC, the non-alcoholic ready-to-drink industry can grow about 5% p.a. (2% volume and 2-3% price/mix), underpinned by long-term fundamental growth drivers: population growth; urbanisation; and the rising income available to the middle classes. However, for 2016 and 2017, given the macro-economic issues, the company is expecting 4% (volume 2% and price/mix 1-2%).

However, the company believes there is a strong argument for it to gain share

Furthermore, the company believes it has the opportunity to gain share. Currently, the company has a value share of 1/3rd but this is made up of a higher than 50% share in the sparkling category but only 15% in still (of which 20% in juice). The company is expected to develop both still and sparkling brands, organically (innovations like Simply Orange); through acquisitions (for instance, SmartWater) and joint ventures (it has an incubator fund which allows it to take full control if successful, e.g. Honest Tea). Indeed, it continues to invest in new growth platforms – from energy drinks (transaction with Monster Beverage Corporation) and at-home beverage dispensing systems (Keurig KOLD – currently discontinued and waiting for a more efficient system), to plant-based protein drinks (via the transaction with China Culiangwang Beverages Holdings), to cold-pressed organic juices (Suja) (Chi in Nigeria is the leading juice and value-added diary company).

Fig. 30: Keurig KOLD at home dispenser system

Source: Keurig

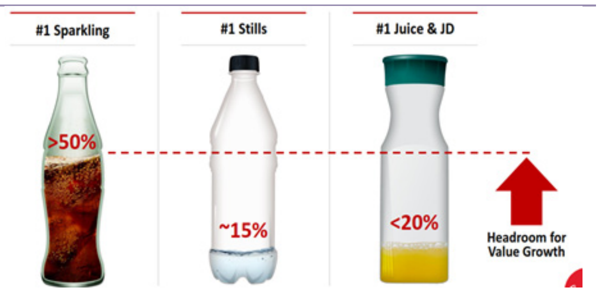
Fig. 31: Suja – organic, non GMO, cold pressed

Source: Suja

Fig. 32: The world's most valuable portfolio of beverages brands (Vvlue share position 2015)

Source: Coca-Cola Cagny presentation, February 2016

Fig. 33: Significant growth potential (2015 value share)



Source: Coca-Cola Cagny presentation, February 2016

During the next 10 years, TCCC's top-line could well average 6.5% p.a.

With non-alcoholic beverages still accounting for nearly 60% of the global market, a growth in share from 15% to 25% over 10 years would bring TCCC's revenue growth for that period to 6.5% instead of 5% for the industry. This type of market share growth is not unrealistic given that in the US the company managed to increase its share in still non-alcoholic beverages to 36% in 2015 from 15% in 2000 (i.e. averaging 1% growth p.a.).

However, to achieve above-industry growth, the company will need to make disciplined portfolio choices in response to the trends amongst consumers:

1) Sugar and choice: TCCC is facing challenges and headwinds around added sugar and total sugar consumption and, as a result, it will need to go from offering choice to shape choice using the ability of its systems, marketing, and reformulations to provide a portfolio that allows consumers to enjoy sugar responsibly. The 'Share a Coke' campaign was already a response to the personalisation trend

and smaller packages for people who wanted to control their calorie intake. But other answers that the company will offer will be not only smaller packs but also innovation (promoting healthier and lighter products). This also fits well with the strategy of being less volume-led (selling 2-litre PET at a discount) to being focused on value (small glass bottle). The new One Brand strategy also evolves around the same: previously, consumers wanting less sugar had to change brand (going to Diet Coke and Coke Zero from Coke Classic), now it is all about the same Coke brand with different varieties.

2) Income and quality: TCCC needs to react to the different economic trends that it observes which is where affordability and premiumisation comes into play, but also relocating resources to those areas where there is a better short-term return, e.g. currently China, Argentina and Venezuela are declining but Indonesia and India continue to grow. In India, the company has developed a new small PET with a longer shelf-life (the problem was that small PET loses gas quicker) to improve the affordability in rural areas. In developed markets, packaging also needs to reflect affordability but at the same time there is a strong trend to premiumise.

3) Strategy in still drinks: TCCC is the number one in sparkling but also number 1 in juice, juice drinks, ready-to-drink coffee and a strong number 2 in most other categories (energy drinks, sports drinks, tea). It has a 50% value share in sparkling beverages but only 15% in still, where it can see opportunities to grow share. Although the industry is growing in both premium and affordable still offerings, Coke sees more growth in the premium stills. To increase its share in this area the company is adding local brands through acquisitions. On top, the company is looking for some of these brands to be scaled globally. Stills were 10% of the portfolio a decade ago and are now 25% and the trend is this figure will continue to rise.

3.5. Financial outlook

TCCC's own guidance is for 4-6% organic net revenue growth, 6-8% organic operating profit growth and high single-digit EPS growth. However, for 2016 and 2017, the company is guiding for somewhat slower top-line growth at 3-4% (volume 1-2% and price/mix 1-2%), given the tougher macro-economic situations in different parts of the world.

In its press release for the Q2 2016 results, the company guided for 2016 organic revenue growth of 3% and reported net revenue decline of 5-7% driven by the divestments impact of 6-7% and currency headwinds of 2-3%. Income before taxes is expected to grow organically by 6-8% (in line with the long-term target) and reported to decline by 4-7% given the headwinds from divestments of 4% and a currency impact of a negative 8 to 9%. With an expected tax rate of 22.5% and a USD2-2.5bn share repurchase programme, the company is expecting full-year EPS to be down 4-7% on last year's USD2 per share. Consensus EPS for 2016 is standing at USD1.91.

Looking further ahead, consensus is expecting growth in EBIT and net income in both 2017 and 2018, despite the further divestments which should be taking place.

Fig. 34: TCCC consensus estimates

USDm	2015	2016e	2017e	2018e	2019e	2020e
Revenues	44,257	41,611	35,591	33,872	35,904	38,059
Growth %		-6.0%	-14.5%	-4.8%	6.0%	6.0%
EBITDA	12,343	12,017	12,245	12,525	13,521	14,407
EBIT	10,373	9,957	10,270	10,996	11,821	12,707
Growth %		-4.0%	3.1%	7.1%	7.5%	7.5%
EBIT margin	23.4%	23.9%	28.9%	32.5%	32.9%	33.4%
Net income	8,797	8,353	8,701	9,271	10,105	11,015
EPS	2.00	1.91	2.01	2.16	2.35	2.57
Growth %		-4.5%	5.2%	7.5%	9.0%	9.0%

Source: IBES

3.6. A deal with Coke makes sense

Access to the largest and iconic soft drink portfolio: Combining the largest alcoholic beverages portfolio with the largest non-alcoholic beverages portfolio would create an unrivalled drinks business with some of the most iconic brands including Budweiser and Coca-Cola.

Further upside from the development of still: The development of the still non-alcoholic drinks business would allow for the soft drinks business to grow at around 6.5% p.a. in terms of top-line which is ahead of the 5.7% annual growth that we expect for the combined AB InBev/SABMiller business.

"We could run it with 200 people"

Cost synergies: We believe that AB InBev will be able to squeeze an additional USD5.9bn (20% of revenues) out of the slimmed down TCCC business based on additional distribution, production, R&D (to develop new products, packaging, plant bottling technology, energy efficiency, etc., which is very much the same as done by AB InBev's R&D), advertising support for the bottlers and corporate costs (USD1.1bn). According to a Bloomberg report from October 2015, 3G Capital's Jorge Paulo Lemann, who partially controls AB InBev, was asked in a closed meeting what his dream acquisition would be, to which he responded Coca-Cola adding "We could run it with 200 people" (instead of the planned 39,000 post the re-franchising).

Distribution synergies: although TCCC is in the process of selling of its last remaining distribution assets, we believe that AB InBev could see significant cost opportunities to re-integrating globally all the Coca-Cola bottlers. Not only does the company continue to have significant stakes in some of the larger bottlers, but there are other levers that AB InBev could use to buy these businesses back (contract for a bottling business has to be renewed every 25 years and pricing of the concentrate is unilaterally determined by TCCC as is the advertising support). Full control of the bottler system will also allow for quicker execution to increase the still drinks portfolio (introducing a new brand in a country can be slow as initial investments are balanced with the bottlers short-term profit targets). We estimate the overall cost opportunity for AB InBev if it owns the entire Coke system at USD18.9bn. Furthermore, adding the entire system to AB InBev's revenues would propel the company to USD165bn and operating profit including all synergies would be USD68.5bn.

The largest Coke and AB InBev shareholders are working together already: Warren Buffet who owns 9% of Coca-Cola has partnered with 3G Capital (AB InBev shareholder) in the buyout of

Heinz Co. Buffett also helped finance 3G's merger of Burger King with Canadian donut chain Tim Hortons, creating Restaurant Brands International. In his last annual letter to Berkshire Hathaway shareholders, Warren Buffet hinted that more ventures are possible and that "Jorge Paulo and his associates could not be better partners. We share with them a passion to buy, build and hold large businesses that satisfy basic needs and desires." Buffett wrote.

Fig. 35: Pros and Cons for AB InBev to acquire TCCC

Pros	Cons
The acquisition would be earnings enhancing by 20% assuming that AB InBev would pay USD70 per share (a 67% premium on the current share price of USD42), could realise USD5.9bn synergies and finance the deal with 55% equity. Any subsequent action to buy out bottlers would not require new equity.	It is a big transaction and an EV of between USD250 and USD300bn might be a step too far.
Combining the largest alcoholic beverages portfolio with the largest non-alcoholic beverages portfolio would create an unrivalled drinks business with some of the most iconic brands including Budweiser and Coca-Cola.	The bigger the company get and more fragmented in terms of brands, the more complex to manage.
The Coke system is stream-lined with TCCC responsible for the back-office, production and global marketing of the portfolio and the bottlers responsible for in-market execution and distribution. This offers AB InBev the opportunity to gradually step up its involvement in the Coke system, through first buying TCCC and afterwards focus on the bottlers as and when it is opportune.	The separation of TCCC from its in-market operations is not always the most efficient as objectives are not always aligned, making the system less nimble to adapt to changing consumer needs. Sources of profit leakage are diverse from R&D (making products, bottlers don't want), to advertising (local needs might vary), to production (TCCC does not control the availability of products or distribution)
Access to TCCC can generate savings in terms of production (move to common sites), distribution of the concentrate and the finished products to the bottlers (scale), advertising (common media buying), R&D, headquarters' costs (a lot of duplication).	TCCC has embarked on its own cost savings plan, taking out USD3bn in the period 2014-2019 (USD0.5bn p.a.), which is 16% of its costs and could always up that significantly (to USD5bn) if it wanted to defend itself against an AB InBev approach.
Potential distribution synergies through merging AB InBev's beer distribution with the distribution in the Coca-Cola system (the bottlers) should be significant. Furthermore because of the power that TCCC has over its bottlers, buying out the bottlers might be not so expensive. This should especially be the case outside the US and in emerging markets where AmBev has proved that combining beer and soft drinks production, distribution and selling can be very profitable.	The distribution channels for beer are slightly different than for soft drinks, especially in the US, where beer is sold more in bars, restaurants and liquor stores while soft drinks are to a large extent a fountain business in restaurants that don't sell beer (e.g. MacDonald's). Nevertheless, there is big overlap in convenience stores. Another drawback in the US is that it might prove difficult to combine AB InBev's 500 independent distributors with the 250 Coca-Cola bottlers. Furthermore in some states combining beer and soft drinks distribution will not be allowed.
Diversifying its portfolio with a wide range of healthier drinks remains key to TCCC's long-term strategy. We calculate that TCCC could grow its top line at 6.5% p.a. for the next ten years, which is well above the company's own guidance of 4-6% and is ahead of the 5.7% revenue growth that we expect from AB InBev after the SABMiller integration.	Saving on the large R&D function could hamper the company's ability to grow organically as it might be less able to develop new products that cater for changing consumer needs. On the other hand, there should be a significant overlap between AB InBev and TCCC on R&D for packaging, energy efficiency, water usage, production and bottling.
Warren Buffet whoh owns 9% of Coca-Cola has partnered with 3G Capital (AB InBev shareholder) in the buyout of Heinz and has partially financed the acquisition of Tim Hortons by BurgerKing. However, Warren Buffet does not like hostile take-overs.	AB InBev could need to divest its Pepsi business in Brazil and Latin America South, but we calculate that together they are USD1.1bn of revenue and USD300m of operating profit. This is ofcourse important and AB InBev will want to keep that as long as it cannot approach the Coca-Cola bottlers in these regions. However, compared to an overall deal value of USD250-300bn, this is relatively small.

Source: Bryan, Garnier & Co ests.

Timing of an approach will be crucial to generate earnings enhancement of 20-30%

We have run a couple of different scenarios including synergies between USD3.0bn (10% acquired revenue) and USD5.9bn (20% acquired revenue – our most likely scenario) and found that, assuming that a serious 35% premium has to be paid on top of an undisturbed share price, a deal will only make sense if AB InBev's shares are at least 3x the share price of TCCC's. This could be the case because of investors' disappointment with the progress and short-term dilution of the Coca-Cola transformation or this could be because of investors' excitement on AB InBev's progress in delivering synergies from the SABMiller transaction supported by a resurgence in emerging market currencies. Depending on the scenario, we calculate that with USD5.1bn of synergies and a share price ratio of 3.3x a TCCC acquisition would enhance earnings by 20-30%.

Fig. 36: Key financial considerations for an acquisition of TCCC

	KO and ABI P/E at 20x and USD3bn synergies	KO and ABI P/E at 20x and USD5.9bn synergies	ABI shares 3.3x KO shares and KO P/E at 20x	ABI shares 3.3x KO shares and KO P/E at 16x
Coca-Cola share price @20x P/E (USD)	52.0	52.0	52.0	41.1
Acquisition premium	15%	35%	35%	34%
Coca-Cola acquisition price (USD)	60.0	70.0	70.0	55.0
Implied TCCC P/E multiple	23.1	26.9	26.9	21.2
Number of shares (bn)	4.0	4.0	4.0	4.0
Market cap	240.0	280.0	280.0	220.0
Net debt	20.0	20.0	20.0	20.0
EV	260.0	300.0	300.0	240.0
EBITDA	12.5	12.5	12.5	12.5
Net profit	10.4	10.4	10.4	10.4
EPS	2.60	2.60	2.60	2.60
AB InBev's share price @20x P/E (USD)	136	136	172	136
Number of shares (bn)	2.0	2.0	2.0	2.0
Market cap	270.6	270.6	342.2	270.6
Net debt	77.0	77.0	77.0	77.0
Other	32.0	32.0	32.0	32.0
EV	379.6	379.6	451.2	379.6
EBITDA	28.0	28.0	28.0	28.0
Net profit	13.5	13.5	13.5	13.5
EPS	6.78	6.78	6.78	6.78
Combined EBITDA	40.5	40.5	40.5	40.5
Synergies	3.0	5.9	5.9	5.9
New EBITDA	43.5	46.4	46.4	46.4
Financing capacity (5x net debt new EBITDA)	218	232	232	232
Existing debt	97	97	97	97
Remaining external financing	121	135	135	135
Equity financing	139.5	165.0	165.0	105.0
Percent stock	54%	55%	55%	44%
Combined net profit with net interest charge of 3%	20	20	20	20
Number of shares (bn)	3.0	3.2	3.0	2.8
New EPS	6.72	6.19	6.72	7.18
Dilution	-1%	-9%	-1%	6%
Synergies	3.0	5.9	5.9	5.9
Synergies % acquired revenue	10%	20%	20%	20%
Combined net profit incl. synergies	23	24	24	24
Number of shares (bn)	3.0	3.2	3.0	2.8
New EPS	7.47	7.57	8.22	8.78
Enhancement	10%	12%	21%	29%

Source: Bryan, Garnier & Co ests.

4. The PepsiCo way

PepsiCo is the alternative acquisition target for AB InBev, which has as an advantage in that the company is a vertically-integrated operational company, whereas TCCC is more of a marketing company using a franchise system (its bottlers). AB InBev would find it probably easier to integrate PepsiCo in terms of volumes, regulations, financing. An acquisition could be set-up together with Kraft Heinz as PepsiCo is not only beverages but even more snacks. We believe that AB InBev would be able to generate USD6.9bn synergies, which are 20% of the acquired PepsiCo beverages business. Because an acquisition would be made entirely with debt, the acquisition would enhance EPS by 40%.

4.1. What is PepsiCo?

9% global market share in non-alcoholic RTDs and 10% in snacks

PepsiCo is one of the biggest food and beverages companies that, through its own operations, authorised bottlers, and contract manufacturers make, market, distribute and sell a wide variety of beverages, foods and snacks (including Frito-Lay, Gatorade, Pepsi-Cola, Quaker and Tropicana) in more than 200 countries. It is the global number two in non-alcoholic RTDs with a 9% volume share and is the global snacks co-leader with a 10% market share (in macro snacks –Nestle also has 10%). However, its position in the US is stronger. For example, in the last quarter (Q3 2016), the company's products made up 37% of all US retail sales growth.

Very active M&A until 2011, including buying back its US bottlers in 2010 and buying Wimm-Bill_Dann in Russia.

In 1965, the Pepsi-Cola Company and Frito-Lay merged to create PepsiCo. Between the late-1970s and the mid-1990s, PepsiCo expanded in a large number of businesses outside its beverages and packaged food brands, but in 1997 it sold or spun off most of them (e.g. Yum!) to focus on its snack food and beverage lines. In these two areas it continued its acquisitions. In 1998, the company acquired the orange juice company Tropicana Products and it merged with Quaker Oats Company in 2001, adding with it the Gatorade sports drink line and other Quaker Oats brands such as Chewy Granola Bars and Aunt Jemima.

In 2010, PepsiCo completed the USD7bn acquisition of its two largest bottlers in North America: Pepsi Bottling Group and PepsiAmericas. In February 2011, the company spent USD3.8bn on a 66% stake in Wimm-Bill-Dann Foods, a Russian food company that produces milk, yogurt, fruit juices, and dairy products, and bought the rest in October 2011. In 2011, the company also bought the Brazilian cookie and cracker maker Grupo Mabel for about USD450m. But since, there has not been much M&A activity except for two joint ventures (2011 JV with Tingyi for the Chinese market and 2012 US dairy JV with the Theo Muller Group, the latter having meanwhile ended).

External growth has been non-existent over the past five years because it cannot work the maths.

At Cagny in New York (18/2/2016), chairman and CEO Indra Nooyi explained that the company is finding it hard to find the right opportunities. "The small ones are just excessively priced because everybody wants to go after them. And the big ones each have their warts, whether it is management team not there, the business model doesn't fit or it is a conflict of what we're doing in our own strategy. So we have yet to find that gem of a company out there that we think can meaningfully create value and grow PepsiCo better than what we are doing today. So there is nothing out there at the moment." Nevertheless, PepsiCo seems to be looking at most opportunities and indeed has some targets (e.g. reaching USD30bn in revenue from "everyday nutrition" from USD17bn currently), which cannot be met without acquisitions. One opportunity the company is interested in is the good food strategy, adding distribution and increasing scale. However, the stumbling block seems to be that it is setting the bar for ROIC accretion relatively high (with core net ROIC at 19.6%), and in doing so, we believe, is hampering its future growth.

But the company has the firepower for a USD50bn acquisition.

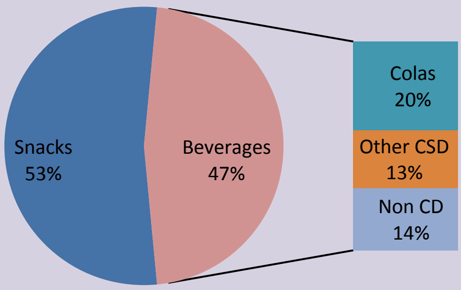
In the meantime, the company has hardly any debt (at the end of 2015 we calculated USD16.3bn net debt on EBITDA of USD10.7bn) and continues to generate USD8bn of free cash flow p.a. (used to buy back shares and dividends of USD9bn in 2015). We calculate that the company could potentially make a USD50bn acquisition, which is sizeable, compared to its current USD155bn market cap.

Revenues are split between 53% snacks and 47% beverages

PepsiCo's net revenues consisted in 2015 of 53% snacks and 47% beverages. We estimate that about 20% of the groups' revenues are colas and another 13% other CSD. Non-carbonated drinks (juices, teas, RTDs etc) account for an estimated 14%.

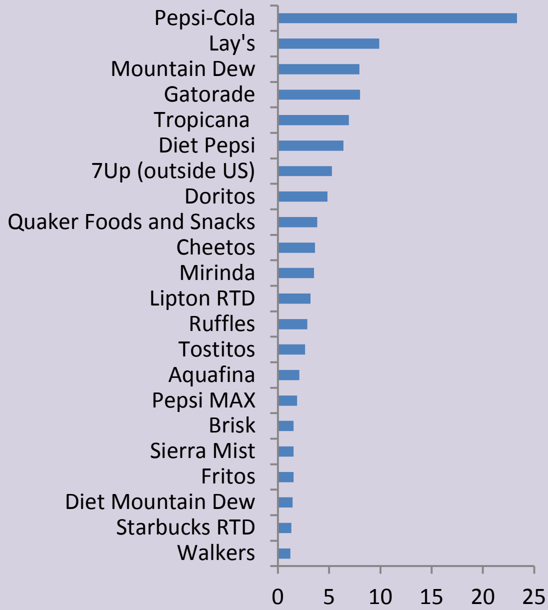
Overall, the company has 22 one-billion USD brands (generating more than USD1bn annual retail sales) including: Pepsi, Lay's, Mountain Dew, Gatorade, Tropicana, 7 Up, Doritos, Lipton Teas, Quaker Foods, Cheetos, Mirinda, Ruffles, Aquafina, Pepsi Max, Tostitos, Mist Twist, Fritos, and Walkers.

Net revenue by segment, 2015



Source: PepsiCo

22 one billion brands (USD bn, 2015e)

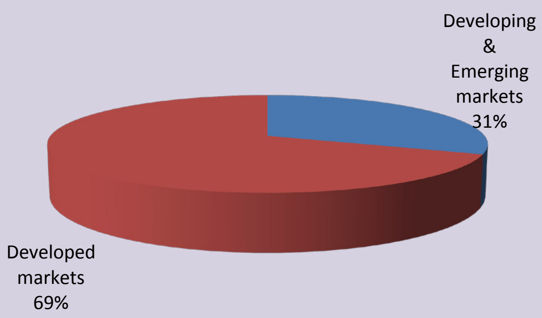


Source: Bryan, Garnier & Co ests

Mostly developed markets business and 75% of net revenues is made in 5 countries

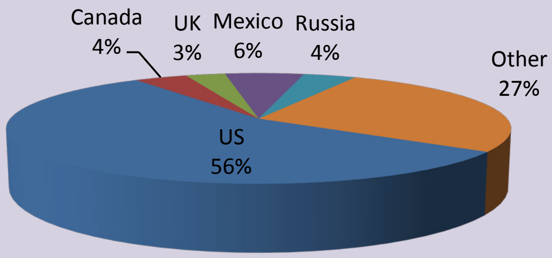
The company's business is mostly geared towards the developed markets which account for 69% of net revenue and the developing & emerging markets for 31%, reflecting the company's late entry in these markets (it is an estimated 41% for the Coca-Cola system). Overall, 75% of net revenues is made in only five countries, but over 90% of the developed markets revenue is made in only three countries: the US is the biggest market accounting for 56% of net revenue and the Canadian and UK markets account for 4% and 3% respectively. The two most important developing markets are Mexico (6% of net revenues) and Russia (4%).

Fig. 37: Net revenue by geography, 2015



Source: PepsiCo

Fig. 38: 75% of net revenues made in 5 countries, 2015



Source: PepsiCo

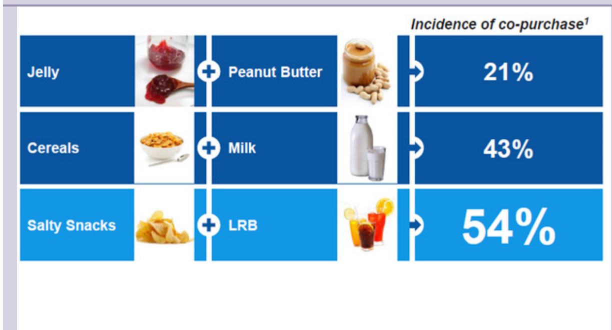
4.2. How does Pepsi make its money?

Fully integrated snack and beverages business generates cost efficiencies and cross-selling opportunities

The key for PepsiCo is that it has integrated snacks and beverages. This integration finds its origins in the high coincidence of purchases between the two categories. According to market research from IRI (Information Resources, Inc.), 54% of US consumers who buy salty snacks also buy a beverage in the same basket. For instance, PepsiCo states that when Frito-Lay snacks are merchandised along with Pepsi carbonated soft drinks (or CSDs), it results in higher sales. Another interesting observation is that more than 60% of US households who buy Mountain Dew also buy Doritos tortilla chips. But being in both categories also delivers significant financial benefits and opportunities like:

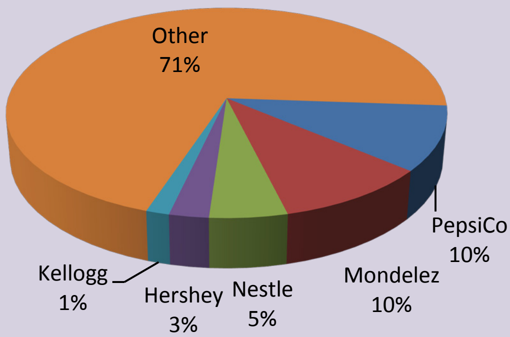
- Cross-selling opportunities, as a strong presence in one of the categories in a region makes the entry easier for the other category. For instance, PepsiCo is able to leverage its beverage business in emerging markets to develop its snacks business.
- Negotiating power with customers: especially in the US, PepsiCo's product portfolio is the most important concentrated portfolio and was representing an estimated 37% of all food and beverage retail sales growth, significantly higher than its US food and beverage dollar share position of less than 10%.
- Fully-integrated distribution allows for the most efficient use of transport.
- A common function for purchasing ingredients for both beverages and snacks

Fig. 39: PepsiCo's complementary product portfolio



Source: IRI

Fig. 40: PepsiCo global macro snack share, 2015



Source: Bryan, Garnier & Co ests

Fully vertically-integrated

For both its snacks and beverages business, PepsiCo is strongly vertically-integrated, which means that it makes, markets, distributes and sells all its brands. This is in contrast to Coca-Cola which is more of a brand-owner/marketing company split from the local marketing, distribution and selling. The argument can be made that PepsiCo is a more operational-oriented company.

PepsiCo owns 75% of its final beverages sales while Coca-Cola drops to only 3%

PepsiCo's beverages operations are similarly structured to Coca-Cola's in the sense that it sells concentrates, fountain syrups and finished goods to authorised bottlers, independent distributors and retailers. Furthermore, the company has two big joint ventures: one with Unilever (for the Lipton Tea RTDs) and one with Starbucks (marketing, sale and distribution of Starbucks' RTD coffee and energy beverages). However, the big difference is that PepsiCo finds more value in holding on to its bottlers as it is convinced that it aligns better the interests of the company, enables it to be quicker and more flexible in delivering products (exactly the same reasons why Coca-Cola wants to separate them). As a result, PepsiCo owns about 75% of final beverages sales (whereas Coca-Cola is moving to 3% by the end of 2017).

4.3. PepsiCo on a mission: Performance with Purpose

Performance with Purpose

PepsiCo's mission statement has been worded by CEO Indra Nooyi as 'Performance with Purpose' and intends to position PepsiCo for long-term, sustainable growth by aligning what is good for its business with what is good for society and the planet. Performance with Purpose is focused on three priorities: human sustainability (improving the nutritional profile of its products while offering more choices to meet changing consumer needs), environmental sustainability (reducing the environmental impact while lowering operating costs), and talent sustainability (continuing to develop a diverse and engaged workforce).

Moreover, the senior management focuses on the framework known as the '5Cs' to guide PepsiCo business strategy and long-term planning: Commercial agenda, building new Capabilities, increasing focus on Costs, fostering a culture of Collaboration, exercise discipline when it comes to Capital returns

4.3.1. Upgrading the commercial agenda

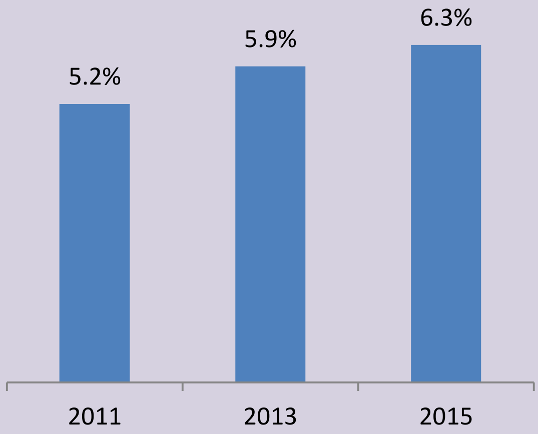
Target of doubling revenues from healthy foods to USD30bn from USD15bn

Much of PepsiCo's commercial agenda involves delivering the types of products consumers demand. And for this, the company wants to do more to capture the health and wellness growth potential. Consumer demand continues to shift towards more nutritious products and, as a result, PepsiCo is accelerating its efforts to meet this demand by reducing salt, added sugars and saturated fat in many of its products while continuing to invest in growing its nutrition businesses. PepsiCo plans on doubling its nutritional business from around USD15bn (approx. 27% of the portfolio in 2015) to USD30bn (the original time frame of 2020 has been abandoned and growth is likely to come not only from organic but also from acquisitive sources). The company has classified its products into three categories: "fun for you" (such as potato chips and regular soda), "better for you" (diet or low-fat versions of snacks and sodas), and "good for you" (items such as oatmeal). Resources are shifting from junk foods into the healthier alternatives and the healthiness of the "fun" offerings is also being improved.

Driving bigger more scaleable ideas

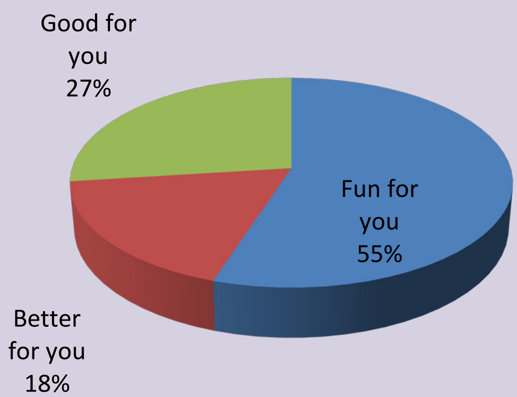
Another part of upgrading the commercial agenda is to lift and adapt ideas across the company to leverage its global scale (driving bigger, more scaleable ideas for its global brands while maintaining local relevance and innovation, e.g. Pepsi emoji's, Maxx deep ridge crisps, Walker Sunbites) and focus on new partnerships and foodservice opportunities (e.g. craft soda Stubborn Soda fountains).

Fig. 41: Investing for growth – advertising and marketing as a % of revenues



Source: Canadean

Fig. 42: PepsiCo's product categories redefined (2016e)



Source: Canadean

Upgrading the commercial agenda is also about increasing exposure to emerging markets where there is good demand for PepsiCo's products. In 2015, sales of snacks in China and Pakistan grew in double-digits and its e-commerce business in China grew even faster.

4.3.2. Building new capabilities

As consumer tastes and preferences continue to evolve, PepsiCo is building new capabilities to meet the demands of its customers and consumers. To that end, it is increasing its e-commerce presence and capabilities, developing its front-selling tools (leveraging mobile technology) and data analytics, enhancing design capabilities, continuing to invest in research. Furthermore, the company continues to develop and refine its revenue management capabilities to convey greater value to its consumers through packaging and price points and promotions that are tailored to the shopping occasion, channel and customer.

4.3.3. Increasing focus on reducing costs

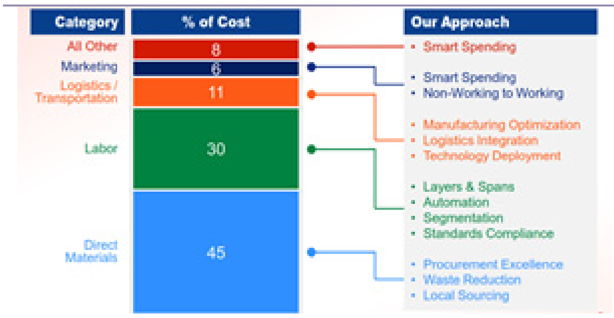
USD1bn cost saving p.a. of which about 1/3rd to go to margin improvement

The company's next priority is improving productivity and lowering the cost base of the company, primarily through leveraging its global capabilities of scale, exploiting automation and advanced technologies and implementing smart spending, which is the PepsiCo version of zero-based budgeting. In 2014, PepsiCo announced its goal of delivering USD5bn in savings over five years from 2015-2019 (USD1bn p.a.). However, not all savings are expected to go to the bottom line. The savings should allow the company to deliver on its promise of 30-50bps operating profit growth p.a., which means that roughly 1/3rd of the savings are used to improve margins and the other 2/3rds is to invest behind the brands.

A snapshot of actions that the company is undertaking include:

- Optimising direct materials cost through a combination of procurement excellence (cheaper buying), reducing usage through improved operational sustainability initiatives (using less) and by increasing local sourcing.
- Labour costs are improved as management layers are reduced, manufacturing and warehousing are automated, and wages are aligned with performance.
- Increasing productivity of logistics, transportation and manufacturing by optimising networks, e.g. products for one market are made on production lines in another, lifting utilisation rates and better integrating the global supply chain.
- And in marketing, effectiveness is increased by shifting more spending to consumer-facing marketing while applying smart spending principles and procurement excellence to many of its marketing activities and vendors.
- Applying smart spending (ZBB) to a broad range of discretionary cost categories. The smart spending idea is being embedded in new behaviours across PepsiCo. For 2016, smart spending is fully implemented across the organisation with significant productivity to be realised across discretionary spending categories including travel and entertainment, sponsorships, consulting and facilities (technical difficulty).

Fig. 43: Addressing USD53bn of global costs



Source: PepsiCo

Fig. 44: New cost management behaviours across PEP

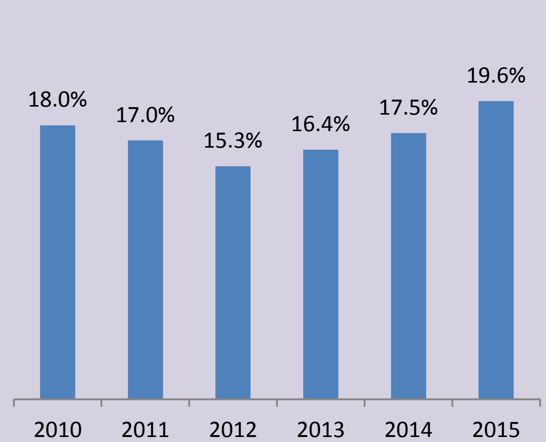
Source: PepsiCo

4.3.4. Exercising discipline with respect to capital returns

ROIC reached 19.6% in 2015 as a result of higher profits and lower capex

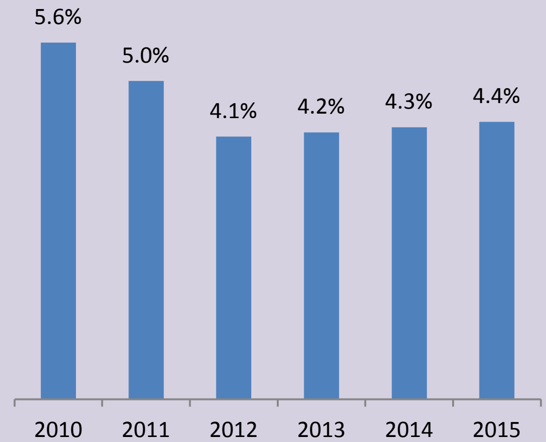
PepsiCo is committed to a disciplined, balanced capital allocation to enhance capital returns. In order to achieve this the company aims to improve capital spending efficiency through a broad menu of initiatives which is allowing for a decline in capital investments as a percentage of sales (-70bps since 2011). One of the ways the company does this is by increasing the capacity utilisation of existing assets. So, for example, PepsiCo extended the productivity of its logistics by increasingly integrating the over-the-road network of its businesses to eliminate any empty miles in the system. In manufacturing, throughput is increased through boosting line productivity. As a result, core net return on invested capital has steadily improved and has increased over 430 basis points since 2012 to 19.6% from 15.3%. The decline before 2011 from 30% in 2007 to 17% in 2011 was mainly because of acquisitions.

Fig. 45: Core net ROIC improvement



Source: Canadean

Fig. 46: Capital spending as a % of revenues



Source: Canadean

The discipline on capital returns also extends to mergers and acquisitions. Earlier we quoted CEO Indra Nooyi explaining that it couldn't find anything that could create value and growth above what PepsiCo already has today. Nevertheless, PepsiCo has today 22 one billion dollar brands because of the past acquisitions which allowed it access to competencies and infrastructure, offered the opportunity to reduce costs and achieve organic growth through cross selling. In some cases, the company has been able to tap new products or infrastructure through forming strategic alliances. Specifically, strategic partnerships have been formed with Tingyi in China in order to claim a share in the growing beverage market in China, and with Tata in India to enhance drinking water manufacturing capabilities. The strategic alliance with Starbucks allowed it to benefit from the growth in the energy drink segment.

4.3.5. Fostering a winning culture

PepsiCo's CEO Indra Nooyi has been developing and promoting the idea of One PepsiCo, which means that individual brands are increasingly associated with the PepsiCo company's values and philosophy of "Performance with Purpose" which is focused on three priorities: human sustainability (e.g. promoting healthier options in the PepsiCo range), environmental sustainability (e.g. reducing water usage by 20%), and talent sustainability (continuing to develop a diverse and engaged workforce). On the latter aspect, a culture of a "can-do spirit" with "a must-do sense of responsibility and accountability" is being promoted: 1) making sure pay is aligned with performance and that true excellence is rewarded; 2) cultivating efficiency and accountability; and 3) driving collaboration across functions in geographic business units.

4.4. Looking for 4% revenue growth

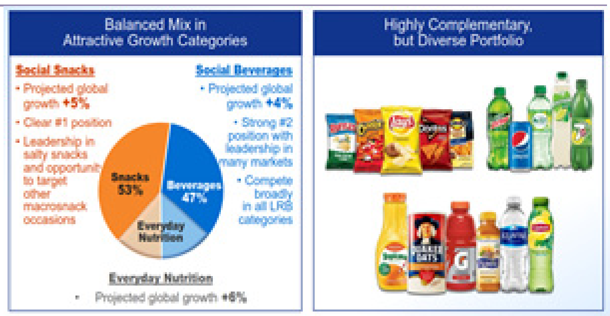
Expected long-term growth rates in non-alcoholic RTDs of 4%, snacks 5% and every day nutrition 6%

With industry growth in the medium term in non-alcoholic beverages expected to be 4%, in snacks at 5% and in everyday nutrition to be 6% (source: IRI, Nielsen), the long-term top-line growth of PepsiCo is expected to be mid single-digit. For PepsiCo, operations outside the United States, particularly Mexico, Russia, Canada, the UK, Brazil, India and China are expected to contribute significantly to revenue growth and profitability.

Fig. 47: Deliver attractive returns

Source: PepsiCo

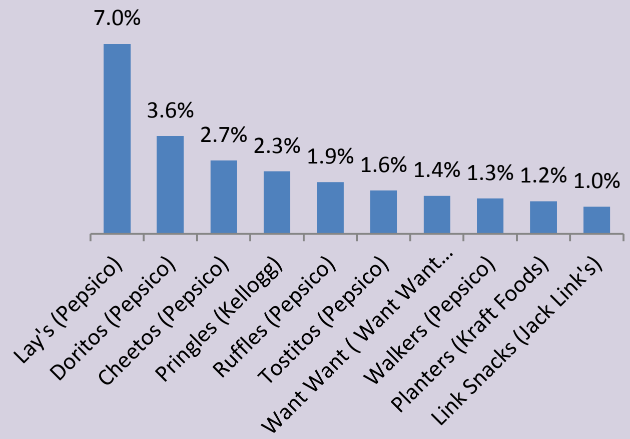
Fig. 48: Strong position in growth categories



Source: PepsiCo

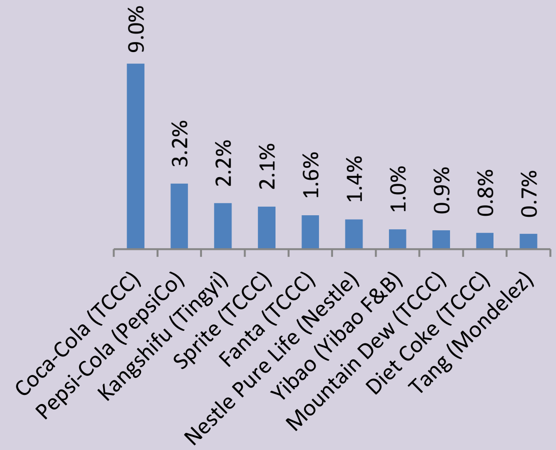
PepsiCo holds 6 out of the top 10 global snack brands: Lay's, Doritos and Cheetos are in the top 3 and Ruffles, Tostitos and Walkers are the other 3 brands in the top 10. It owns only one non-alcoholic beverage in the top 10: Pepsi-Cola. Below, we have identified some of the trends in the snack and beverages industry.

Fig. 49: Global top 10 snack brands,2013



Source: Euromonitor

Fig. 50: Global top 10 non-alcoholic beverages, 2015



Source: Canadean

4.4.1. Healthier snacks and beverages

One trend amongst consumers is the demand for healthier snacks and beverages. Products with added healthier ingredients such as oats, superfruits and grains have been strong performers. As snacks now frequently serve as a "fuel" inbetween meals, or as a replacement altogether, consumers want nutritious snacks that also taste good. The same holds for beverages with the traditional CSD being branded as "a thing of the past," according to PepsiCo's CEO Nooyi (declining 1-2% in volume every year), healthier alternatives that promise energy and nutrition with fewer calories are taking share. In this category are the fruit juices, tea and coffee RTDs, water.

4.4.2. Snacks as a meal replacement

Millennials snack during typical meal times. In the US, 7.5% of millennials eat a snack during breakfast, which is nearly twice as often as any other generation compared to 4.4% for generation X, 2.8% of boomers and 2.9% of adults older than 63. At lunch, 16.6% of millennials eat snacks and 16.2% at dinner (Euromonitor). This also benefits high protein snacks which are perceived as more filling.

Fig. 51: Nature Valley with protein

Source: PepsiCo

Fig. 52: Quaker oatmeal squares

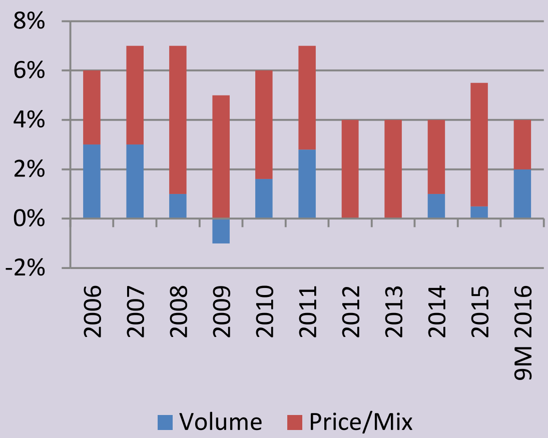
Source: PepsiCo

4.4.3. Premiumisation

Underlying trend of 4% organic revenue growth of which 2% volume and 2% price/mix

Healthier more convenient snacks and beverages tend to be more expensive which improves mix, but also de-emphasises pricing as a driver. As a result, the pricing environment for snacks and beverages has been much healthier over the past five years (visible price/mix has continued to improve by around 4% but that has been mainly driven by Venezuelan inflation). The underlying trend has more been one of 2% volume growth and 2% price/mix, which has been the case so far in 2016. And going forward, this trend should continue with premium snacks and beverages drawing more consumers in both developed and developing markets. PepsiCo is using a whole range of tactics to more expensive products: single-serve bottles, mini cans, aluminium bottles, craft sodas (such as with PepsiCo's recently introduced Caleb's and 1893 whose names refer to the invention of Pepsi by Caleb Bradham in 1893).

Fig. 53: Components of organic revenue growth



Source: Canadean

Fig. 54: 1893 craft kola

Source: PepsiCo

4.4.4. Long-term trend of increased consumption in emerging markets

Volume growth for PepsiCo (and most of the snack and beverages industry) has been disappointing over the past eight years and to a large extent this is because the macro-economic conditions in developing and emerging markets have been subdued. However, long-term trends of rising younger populations, growth in the middle class and growth in consumption per capita remain intact.

4.5. Financial outlook

9 months in line with long-term guidance

After nine months, the company has continued to grow it top-line organically by 4% (of which volume was 2.5% in snacks and 2% in beverages). However reported net revenue declined 2.7% (foreign exchange translation had a 4% unfavourable impact and the Venezuela deconsolidation had a 2.5% unfavourable impact). In the period, reported operating profit increased 21% (reflecting the 20% impact of the 2015 Venezuela impairment charges) and core constant currency operating profit increased 5% (the Venezuela deconsolidation had a 3% unfavourable impact on core operating profit growth). Core EPS was USD3.65, an increase of 4% from the prior year. Excluding the impact of foreign exchange translation, core constant currency EPS increased 7%.

The company has also provided guidance for 2016 for which it expects 4% organic revenue growth, excluding the impact of the 53rd week and structural changes, including the deconsolidation of the Venezuelan operations; based on exchange rates at the end of September 2016 which should negatively impact reported net revenue growth by approximately 3 percentage points; the 53rd week contributing approximately 1% to reported net revenue growth. It also expects EPS of USD4.78 based on 10% core constant currency EPS growth, a negative impact of the Venezuelan deconsolidation of 2% and a negative impact of the strong USD of 3%.

Long-term guidance of mid single-digit revenue growth and 30-50bps margin expansion p.a.

All these figures fit well into the company's longer term guidance for mid single-digit organic revenue growth (+4% after 9 months) and operating margin expansion of 30-50bps p.a. (9 months 2016 operating margin of 17.1% v 16.8%) to deliver constant currency EPS growth of a high single-digit (+10% after 9 months).

Fig. 55: PepsiCo Consensus

USDm	2015	2016e	2017e	2018e	2019e	2020e
Revenues	63,056	62,742	64,808	67,187	69,557	69,453
Growth %		-0.5%	3.3%	3.7%	3.5%	-0.1%
EBITDA	12,353	12,653	13,402	14,203	14,910	15,962
EBIT	9,937	10,263	10,912	11,532	11,971	12,627
Growth %		3.3%	6.3%	5.7%	3.8%	5.5%
EBIT margin	15.8%	16.4%	16.8%	17.2%	17.2%	18.2%
net income	6,788	6,901	7,407	7,883	8,335	8,915
EPS	4.57	4.77	5.16	5.61	6.11	6.67
Growth %		4.4%	8.2%	8.7%	8.9%	9.2%

Source: IBES

4.6. Why should AB InBev be interested in Pepsi?

A combination would create a global brand power house. Combining the largest brewer with the second largest soft drinks company would create a dominant beverages company, enabling it to leverage its size to customers and to suppliers.

They are already working together

They know each other and are already working closely together: Back in 2009, the two companies agreed to combine, in the US, the purchasing of travel, computers and office supplies. At that time, there was already some speculation that this could lead to a combination of the two. In 2010, they combined negotiations on media spending (not advertising or even media planning). In 2013, the two companies developed joint promotions and an in-store marketing campaign aimed at boosting sales of both Budweiser and Pepsi in the run-up to the Super Bowl.

AB InBev already sells PepsiCo products across Latin America. AB InBev's Brazilian subsidiary sells both beers and soft drinks across Latin America. In Brazil, 31% of the soft drinks volumes are PepsiCo products (Pepsi Cola, Gatorade in the isotonic market, H2OH! in the flavoured water market, and Lipton Iced Tea in the ready-to-drink tea market). The other 69% are AmBev's own products like Guaraná Antarctica and Fusion but also other licenced brands like Monster. Furthermore, PepsiCo products are nearly 65% of its soft drinks sales volumes in the Dominican Republic, and all soft drinks volumes in Argentina, Bolivia and Uruguay. For the company as a whole, about 50% of soft drinks volumes are from PepsiCo (i.e. about 22m hl of which 9m hl in Brazil). In Brazil, the PepsiCo franchise agreement expires in 2017 but will be automatically renewed for an additional ten-year term if certain conditions set forth in the agreement are met (exactly which conditions are not disclosed). In Brazil, TCCC's family of brands had a 60.7% market share in the CSD market, while AmBev had a 19.1% market share (with PepsiCo and own products).

Same cultural vision

Both companies have similar cultural visions. Different aspects of both company cultures are very similar: drive to create a better world, employee remuneration according to success, zero-based budgeting.

Activist investor Nelson Pelz want(ed) a deal. Activist investor Nelson Peltz has been calling to break up PepsiCo into two companies. PepsiCo's board and CEO have been able to rebuff him, but an approach from AB InBev would open the doors for a spin-off of the snacks business (or a joint approach from AB InBev and Kraft Heinz, both 3G companies, could enable a more attractive deal for both). However, the question is if PepsiCo has been able to demonstrate to Peltz if the integration between beverages and snacks will be difficult to undo. Meanwhile, Peltz has sold his holding in PepsiCo.

Addressable cost base of USD53bn for PepsiCo vs USD19bn for TCCC

PepsiCo would allow a greater pool of costs to work with. AB InBev's strength in cost-cutting and distribution is particularly geared towards volume businesses like PepsiCo and TCCC. However, PepsiCo owns 75% of its system-wide beverages business, whereas TCCC controls only 3% (by the end of 2017) of the Coca-Cola system. As a result, the USD53bn addressable cost base of the PepsiCo beverages business is significantly larger and could offer more opportunities than the USD19bn from TCCC. Nevertheless, in some key markets such as Mexico, China, India, Canada and Brazil, PepsiCo does not own the businesses and will have to depend on third parties to distribute and penetrate the market. The markets where it does not own the business completely are mainly in the emerging markets as many of these markets have been entered well behind competitors and working with third parties has enabled them to get a large scale distribution quickly.

Fig. 56: Pro and Con's for AB InBev to acquire PepsiCo

Pros	Cons
AB InBev and PepsiCo have to a large extent the same vision for a better world. But both are very hard working on improving profits with tools like ZBB.	Because of its late entry in the emerging markets, they only represent 31% of net revenues (it is an estimated to be 41% at TCCC).
AB InBev and PepsiCo know each other. Not only do they work together in purchasing travel, computers, office supplies, media time; AB InBev is already a Pepsi bottler in Latin America.	PepsiCo has an integrated snack and beverages model, which will cause dissynergies if separated. Although activist Pelz initially attempted a separation, he himself seemed quickly convinced of the merits of integration. We believe that AB InBev will not want to enter the snacks business.
PepsiCo is the complete package: 75% of beverages sales are done by bottlers that it owns completely, so there is less need for a further squeeze out to gain access to distribution synergies	Buying PepsiCo would mean that AB InBev has conceded that it will always be the number 2 soft drinks company, having experienced in Brazil that closing the gap with Coca-Cola is difficult.

Source: Bryan, Garnier & Co ests.

A PepsiCo acquisition could enhance earnings by 40% mainly because it will be fully debt-funded (and together with Kraft Heinz) and synergies of USD6.9bn (20% of revenues)

Below we have calculated the financial benefits for AB InBev to acquire PepsiCo. First, we assume that PepsiCo would be acquired by both AB InBev and Kraft Heinz and that they split the company according to the respective contribution from Beverages and Snacks to the operating profit. Although Beverages takes 47% of revenues, we calculate that they contribute 36% to the operating profit, which implies an EBIT margin of Beverages of 13.6% by 2020. Given that PepsiCo is a 75% fully-integrated soft drinks company and 25% a marketing company, we target an operating margin target below AB InBev's of 34% (which is still well below what the company does in its own Brazilin operations (44.3%)). Given a premium on the PepsiCo shares of 36% (i.e. a takeout price of USD167 on the back of an estimated share price of USD122 - 2020 P/E of 20x), we believe that the deal could be financed completely with debt and that there is no need to raise equity. Given the large amount of synergies available, the deal could be immediate earnings enhancing by 41%. This is assuming that there are synergies of 20% of the acquired revenue. But even assuming synergies of 10%, the deal would still be 21% earnings enhancing.

Even if we assume that Kraft Heinz would ask AB InBev to pay more than its fair share based on the operating profit contribution, i.e. a top-line split of 47%, then the deal could still be entirely financed with debt and would be 35% accretive.

Fig. 57: Key financial considerations for an acquisition of PepsiCo

	PEPBev and ABI P/E at 20x and USD3.4n synergies	PEPBev and ABI P/E at 20x and USD3.4bn synergies	PEPBev and ABI P/E at 20x and USD6.9bn synergies	PEPBev and ABI P/E at 20x and USD6.9bn synergies but paying 47% of take-out
PepsiCo Bev share price @20x P/E (USD)	44.0	44.0	44.0	44.0
Acquisition premium	14%	36%	36%	79%
PepsiCo Bev acquisition price (USD)	50.0	60.0	60.0	79.0
Implied PepsiCo Bev P/E multiple	22.4	26.9	26.9	35.4
Number of shares	1.5	1.5	1.5	1.5
Market cap	75.0	90.0	90.0	118.4
Net debt	9.5	9.5	9.5	9.5
EV	84.5	99.5	99.5	128.0
EBITDA	5.5	5.5	5.5	5.5
Net profit	3.4	3.4	3.4	3.4
EPS	2.23	2.23	2.23	2.23
AB InBev's share price @20x P/E (USD)	136	136	136	136
Number of shares	2.0	2.0	2.0	2.0
Market cap	270.6	270.6	270.6	270.6
Net debt	77.0	77.0	77.0	77.0
Other	32.0	32.0	32.0	32.0
EV	379.6	379.6	379.6	379.6
EBITDA	28.0	28.0	28.0	28.0
Net profit	13.5	13.5	13.5	13.5
EPS	6.78	6.78	6.78	6.78
Combined EBITDA	33.5	33.5	33.5	33.5
Synergies	3.4	3.4	6.9	6.9
New EBITDA	36.9	36.9	40.4	40.4
Financing capacity (5x net debt new EBITDA)	184	184	202	202
Existing debt	87	87	87	87
Borrow	85	100	100	128
Equity financing	0.0	0.0	0.0	0.0
Percent stock	0%	0%	0%	0%
Combined net profit with net interest charge of 3%	14	14	14	13
Number of shares (bn)	2.0	2.0	2.0	2.0
New EPS	7.19	6.97	6.97	6.54
Dilution	6%	3%	3%	-4%
Synergies	3.4	3.4	6.9	6.9
Synergies % acquired revenue	10%	10%	20%	20%
Combined net profit incl. synergies	17	16	19	18
Number of shares (bn)	2.0	2.0	2.0	2.0
New EPS	8.47	8.24	9.56	9.13
Enhancement	25%	21%	41%	35%

Source: Company Data; Bryan, Garnier & Co ests.

5. The Coca-Cola Company or PepsiCo

A TCCC acquisition could enhance earnings by 20% and buying PepsiCo by 40%

We calculate that a well-timed acquisition of TCCC, when AB InBev shares trade at a stock price of over 3x (in absolute terms) those of TCCC and that the acquisition is paid for by 55% equity and 45% debt (to bring the company's net debt/EBITDA ratio post acquisition at 5x), a TCCC acquisition could enhance earnings by about 20%. We also assume that synergies run up to 20% of revenues (USD5.9bn). For PepsiCo, we assume that AB InBev finds a partner in Kraft Heinz and acquires it together (in a 36%:64% split reflecting the EBIT contribution of Beverages and Snacks) and will be able to realise synergies of up to 20% in the Beverages division (USD6.9bn), then the deal would enhance AB InBev earnings by about 40%.

However, if AB InBev acquires more Coca-Cola bottlers the total earnings uplift could be 90%

Does that mean that the financial odds are stacked in favour of a PepsiCo deal? Not really. The difference between a TCCC and a PepsiCo deal is that TCCC excludes all bottling business and that PepsiCo sells itself including all bottling revenues (at least 75%). We would argue that bottlers do NOT deserve the same multiple as the brand owner, for the simple reason that the brand owner can often stop a bottling/distribution contract for not performing well, force much higher prices for its concentrate, or stop advertising support. Furthermore, there is also always a change of control clause. If we assume that AB InBev would be able to acquire all the Coke bottlers for about 20x earnings (which is a significant premium to their net asset value), AB InBev would buy an additional USD70bn of revenues at about 1.2x revenue (!), costing USD84bn and fully debt-financed. However, given its experience in Brazil, it could gain access to an additional USD13bn (!) of synergies. Assuming these parameters, a comparable acquisition of TCCC and its bottlers could enhance earnings by 90%! The company's turnover would be about USD300bn.

Fig. 58: Table: so different and so similar/ so similar and so different

Coca-Cola	PepsiCo
Buying TCCC could enhance EPS by 20%. TCCC is a marketing company, brand owner using a franchise model in which it has separated itself from the bottling business. This of'course has made a potential acquisition by AB InBev feasible but limits the amount of synergies to USD5.9bn (20% of revenues). However, in the years afterwards, AB InBev could gradually buy out, relatively cheaply, the bottlers, opening up an additional savings potential of USD13bn.	Buying PepsiCo could boost EPS by 40%. PepsiCo is a vertically-integrated company, owning the majority of its bottling operations (75% of sales to customers). As a result, savings are bigger given AB InBev's expertise in distribution (USD6.9bn or 20% of revenues).
A TCCC acquisition could end up costing USD300bn and would need an USD165bn equity raising (55%) next to USD135bn debt (45%).	Buying the PepsiCo beverages business would be an USD100bn transaction which could be financed with debt.
TCCC is familiar with AB InBev's zero based budgeting technique, which they call zero based work.	PepsiCo has its own version of ZBB, calling it smart spending.
Combining the largest alcoholic beverages portfolio with the largest non-alcoholic beverages portfolio would create an unrivalled drinks business with some of the most iconic brands including Budweiser and Coca-Cola.	Through buying PepsiCo, AB InBev would from the start concede that it cannot become the largest soft drinks company. It has the experience in Brazil that it cannot compete with Coca-Cola. Buying PepsiCo would always leave a taste of "what could have been".
Carbonated soft drinks, in which it has a global market share of over 50%, are 73% of its beverages volumes. The target is to grow share in still soft drinks from the current 15% (in the US it has grown its share in stills to 36% in 2015 from 15% in 2000). If it were to succeed, revenue growth could well be over 6% p.a., ahead of its target of 4-6%.	Carbonated soft drinks are 70% of beverages revenues, and the company has targeted growth in the nutritional beverages business, which it believes are growing at 6% p.a. For the company as a whole, it targets a mid single-digit 4% growth in revenues.
AB InBev and TCCC don't know each other and TCCC could for a variety of reasons not allow this to happen (the main one already defending itself against an AB InBev approach). There are strong rumours that TCCC will not allow AB InBev to scoop up SABMiller's 57% stake in Coca-Cola Beverages Africa, which distributes about 40% of the continent's volumes.	AB InBev and PepsiCo know each other. Not only do they work together in purchasing travel, computers, office supplies, media time; AB InBev is already a Pepsi bottler in some Latin American countries (Brazil, Dominican Republic, Argentina, Bolivia and Uruguay). (Since December 2015 also the bottler for Coke in Barbados.)
Warren Buffet, who is a partner in AB InBev shareholder 3G Capital in a number of transactions, owns 9% of TCCC, but does not like the idea of hostile takeovers.	Beverages (47% of revenues, 36% of operating profit) are integrated with Snacks (53% of revenue and 64% of operating profit and will need to be separated. This might be easier said than done. Activist Peltz initially supported this idea but has been convinced that keeping them together works better. He has sold his PepsiCo shares.

Source: Bryan, Garnier & Co ests.

Fig. 59: Bottles of Coke for sale in a South African supermarket	Fig. 60: AmBev sells Pepsi in Brazil
	
Source: Bloomberg	*Source: AmBev*

We have also compared the financial performance of TCCC and PepsiCo with AB InBev's and conclude:

Growth profile of beer and soft drinks is the same

1. **Soft drinks have a similar revenue growth profile as beer:** Organic revenue growth at TCCC has averaged 5% in the past 10 years and 6% at PepsiCo. At AB InBev, it was 5% but with the integration of SABMiller this might move up to 6% (SABMiller averaged 7% in the past 10 years).

Soft drinks deliver the same operating margin (although AB InBev's stands out amongst brewers)

2. **Soft drinks tend to deliver the same margins as beer:** Operating profit margins at TCCC are 20% and at PepsiCo 15%. However, TCCC is more a franchise-based operation and if we include all distribution, we estimate margins in the Coca-Cola system at 16%. This is very similar to what most brewers are capable of doing. However, AB InBev's operating margin of 32% has much to do about how the company is being managed.

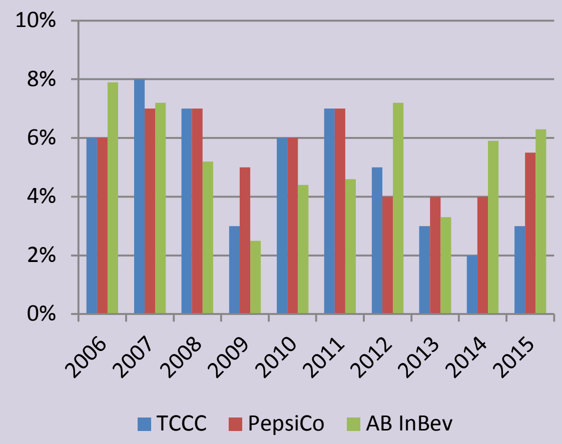
AB InBev's financial performance has been well ahead of TCCC and PepsiCo

3. **Operating profit growth has been difficult at TCCC and PepsiCo:** Ten years ago, PepsiCo and TCCC were making 60% more operating profit than AB InBev. However, now AB InBev makes 60% more than TCCC and 40% more than PepsiCo. Clearly M&A plays a significant role, but even if we adjust AB InBev's figures for the capital increase following the big Anheuser Bush transaction in 2008, AB InBev has grown its operating profit on average by 8% p.a. (on a constant capital base) whereas TCCC managed 3% and PepsiCo 4% (i.e. less than their organic top-line growth!).

AB InBev 10y EPS growth of 10% is well ahead the 4% at TCCC and 3% at PepsiCo

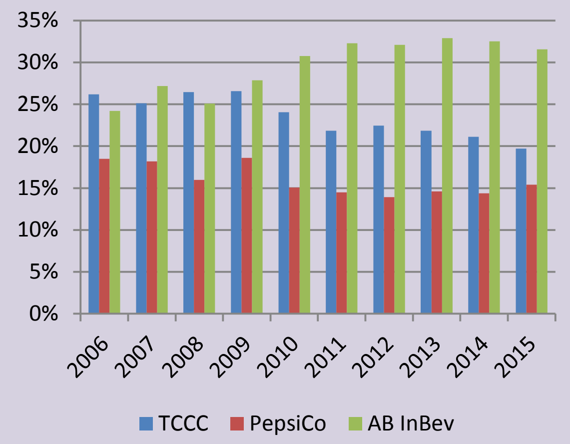
4. **EPS growth says it all:** Combining acquisitions, efficiency improvements and organic revenue growth has delivered for AB InBev shareholders an average growth in EPS of 10% p.a., which is well ahead of the 4% at TCCC and 3% at PepsiCo.

Fig. 61: Organic revenue growth



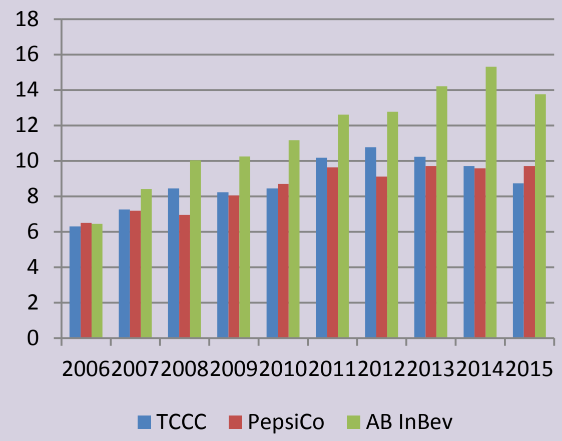
Source: Bryan, Garnier & Co ests.

Fig. 62: Operating margins



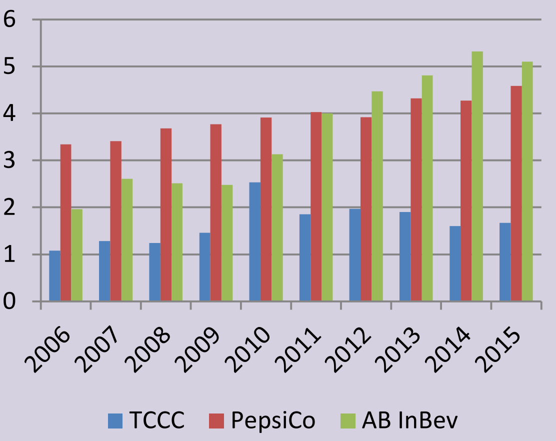
Source: Bryan, Garnier & Co ests.

Fig. 63: Operating profit (USDbn)



Source: Bryan, Garnier & Co ests.

Fig. 64: EPS (USD)



Source: Bryan, Garnier & Co ests.

6. Changes in earnings forecasts and DCF valuation

We have adjusted our revenue and profit outlook given the strength in some of the emerging market currencies against the USD (BRL +25%, ZAR +20%, COP+15%), but also the EUR has rebounded against the USD (+3%). We are increasing our 2017 operating profit and EPS by about 4%.

	FY2016e				FY2017e				FY2018e			
USDm	Old	New	% chge	% Incr.	Old	New	% chge	% Incr.	Old	New	% chge	% Incr.
Revenues	43,637	43,044	-1.4%	-1.3%	57,450	58,284	1.5%	35.4%	60,128	60,870	1.2%	4.4%
North America	15,910	15,743	-1.0%	0.9%	16,181	16,011	-1.0%	1.7%	16,488	16,315	-1.0%	1.9%
Latin America	15,845	15,579	-1.7%	-5.6%	16,645	16,890	1.5%	8.4%	17,682	17,653	-0.2%	4.5%
Europe	4078	3,974	-2.6%	-0.9%	4107	4,235	3.1%	6.6%	4137	4,278	3.4%	1.0%
Asia Pacific	5,777	5,722	-1.0%	3.0%	6,066	6,008	-1.0%	5.0%	6,369	6,308	-1.0%	5.0%
SABMiller					12,324	13,013	5.6%	na	13,219	14,082	6.5%	8.2%
Global export and holding companies	2,025	2,025	0.0%	5.0%	2,127	2,127	0.0%	5.0%	2,233	2,233	0.0%	5.0%
Operating profit	13,575	13,565	-0.1%	-1.5%	19,148	19,891	3.9%	46.6%	20,886	21,609	3.5%	8.6%
North America	5,634	5,654	0.4%	4.4%	5,791	5,811	0.3%	2.8%	5,977	5,996	0.3%	3.2%
Latin America	6,601	6,678	1.2%	-5.7%	6,973	7,348	5.4%	10.0%	7,480	7,773	3.9%	5.8%
Europe	760	741	-2.6%	-0.9%	770	794	3.1%	7.1%	780	806	3.4%	1.5%
Asia Pacific	783	776	-1.0%	4.5%	854	846	-1.0%	9.1%	930	921	-1.0%	8.9%
SABMiller					4,967	5,384	8.4%	na	5,929	6,412	8.1%	19.1%
Global export and holding companies	-203	-284	40.0%	27.2%	-206	-291	41.2%	2.8%	-210	-299	42.6%	2.7%
Nonrecurring items	0	0	na	na	0	0	na	na	0	0	na	na
operating profit margin	31.1%	31.5%			33.3%	34.1%			34.7%	35.5%		
North America	35.4%	35.9%			35.8%	36.3%			36.2%	36.8%		
Latin America	41.7%	42.9%			41.9%	43.5%			42.3%	44.0%		
Europe	18.6%	18.6%			18.7%	18.7%			18.8%	18.8%		
Asia Pacific	13.6%	13.6%			14.1%	14.1%			14.6%	14.6%		
SABMiller					40.3%	41.4%			44.9%	45.5%		
Net interest	(3,986)	(3,989)	0.1%	174.5%	(3,542)	(3,539)	-0.1%	-11.3%	(3,517)	(3,483)	-1.0%	-1.6%
PBT	9,589	9,576	-0.1%	-23.2%	15,607	16,352	4.8%	70.8%	17,369	18,126	4.4%	10.8%
Tax	(2,110)	(2,107)	-0.1%	-18.7%	(3,434)	(3,598)	4.8%	70.8%	(3,995)	(4,169)	4.4%	15.9%
Minority interests	(1,457)	(1,492)	2.3%	-6.4%	(1,553)	(1,679)	8.1%	12.6%	(1,691)	(1,793)	6.0%	6.8%
Net profit	6,022	5,978	-0.7%	-27.8%	10,620	11,076	4.3%	85.3%	11,683	12,164	4.1%	9.8%
Net profit - adjusted	7,577	7,532	-0.6%	-11.5%	10,667	11,123	4.3%	47.7%	11,729	12,210	4.1%	9.8%
Number of fully diluted shares	1,668	1,668	0.0%	0.0%	1,994	1,994	0.0%	19.5%	1,994	1,994	0.0%	0.0%
Diluted EPS - adjusted	4.54	4.52	-0.6%	-11.5%	5.35	5.58	4.3%	23.5%	5.88	6.12	4.1%	9.8%
Net dividend (EUR)	2.38	2.37	-0.6%	-11.5%	2.81	2.93	4.3%	23.5%	3.09	3.21	4.1%	9.8%

DCF based fair value of EUR124

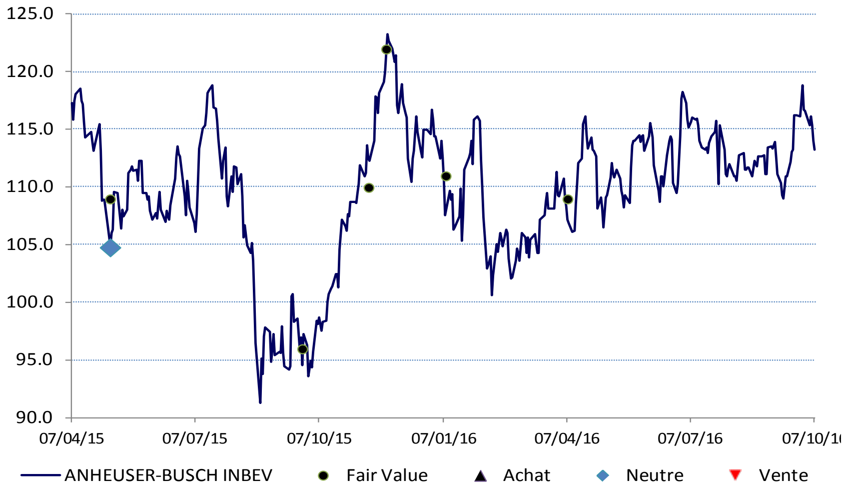
Using a risk free rate of 1.6%, a risk premium of 7%, and a Beta of 0.95, we derive for AB InBev a fair value of EUR124 per share assuming a long-term growth rate of 3.7%

Fig. 65: DCF Valuation

	Dec-16e	Dec-17e	Dec-18e	Dec-19e	Dec-20e	Dec-21e	Dec-22e	Dec-23e	Dec-24e
Sales	43,044	58,284	60,870	63,547	66,381	69,381	72,498	75,421	78,414
EBIT	13,565	19,891	21,609	23,373	24,657	26,042	27,459	28,742	29,978
Tax rate	22.0%	22.0%	23.0%	24.0%	24.0%	24.0%	24.0%	24.0%	24.0%
Taxes	(2,984)	(4,376)	(4,970)	(5,610)	(5,918)	(6,250)	(6,590)	(6,898)	(7,195)
Operating profit after taxes	10,580	15,515	16,639	17,763	18,739	19,792	20,868	21,844	22,783
+ Depreciations	3,078	3,955	4,079	4,202	4,330	4,462	4,600	4,722	
-Investments in fixed assets	(4,038)	(5,333)	(5,416)	(5,567)	(5,725)	(5,891)	(6,054)	(6,199)	
Total net investments in fixed assets	(960)	(1,378)	(1,337)	(1,365)	(1,395)	(1,429)	(1,455)	(1,476)	0
-Investments in working capital	(521)	724	2,298	3,612	2,058	2,151	2,248	2,339	2,432
=Operating cash flow	9,100	14,862	17,600	20,010	19,402	20,514	21,662	22,707	25,215
Discount factor	1.00	0.93	0.87	0.79	0.72	0.65	0.60	0.54	0.49
Present value of free cash flow	9,100	13,876	15,341	15,856	13,977	13,434	12,896	12,289	12,406
Cumulative present value of free cash flow	119,175								
+Present value of terminal value	282,749								
=Enterprise value	401,924								
Adjusted net debt incl pension provisions (restated cash)	(87,510)			Risk free		1.6%			
Other liabilities and commitments				Equity premium		7.0%			
Revalued minority interests	(36,009)			Unlevered Beta		0.95			
(Assoc. + revalued investments)	110			RRE		8.3%			
=Fair value	278,515			LT Growth		3.7%			
Fair value fully diluted per share	140			LT WACC		8.3%			
Fair value fully diluted per share (EUR)	124								

Price Chart and Rating History

AB InBev



Ratings

Date	Ratings	Price
05/05/15	NEUTRAL	EUR108.8

Target Price

Date	Target price
07/04/16	EUR109
08/01/16	EUR111
25/11/15	EUR122
12/11/15	EUR110
24/09/15	EUR96
05/05/15	EUR109

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Stock rating

BUY	Positive opinion for a stock where we expect a favourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential upside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
NEUTRAL	Opinion recommending not to trade in a stock short-term, neither as a BUYER or a SELLER, due to a specific set of factors. This view is intended to be temporary. It may reflect different situations, but in particular those where a fair value shows no significant potential or where an upcoming binary event constitutes a high-risk that is difficult to quantify. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
SELL	Negative opinion for a stock where we expect an unfavourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential downside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.

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