COFFEE-INFUSED COKE? YES PLEASE!

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CASE DESCRIPTION

The subject of coffee on its own boasts many different avenues for study and discussion. But when coffee is combined with the multi-national beverage corporation Coke, topics and options to approach a case become innumerable. Instructors will have plenty of opportunities to engage students and boost participation. This case is ideal for a junior or senior class on branding, marketing strategy, retailing, green marketing, or principles of marketing. It is designed to stimulate discussion about marketing and growth strategies, globalization, merges and acquisitions, positioning, and retail footprint. This case is an excellent vehicle for demonstrating how a single growth decision by a major player can send shockwaves through an entire industry. The case is designed to be taught in a 60-75 minute class, and is expected to require 3 hours of outside preparation by students.

CASE SYNOPSIS

Coffee is a majestic beverage that can quite possibly connect the world together. The Coca-Cola Company is the world's largest beverage corporation, offering over 500 brands to consumers in 200 countries. However, Coca-Cola has not had a hot drink in its product mix, nor has it had a major retail footprint. With the growth in coffee and hot beverages, the company felt that the timing was right for it to make a thoughtful and significant investment in that category. In August 2018, Coca-Cola paid £3.9 or $5.1 billion to buy the U.K.-based coffee company, Costa, giving Coke its entry into the hot drink market. The obvious objective is to tap into the coffee market – mostly with the aim of debuting new products, as sales of carbonated soft drinks (CSD) are down while coffee is up.

Costa Coffee has almost 4,000 stores (approximately 2,500 in England and 1,500 in Europe, Asia, and Africa). Additionally, the company owns and operates 8,000-plus fresh espresso-based vending machines, called Costa Express (mostly in Europe). The U.S. is the largest coffee market in the world, and Americans drink 450 million cups of coffee daily. Costa does not have any stores in the U.S., and the brand is not known to American consumers. However, the surprise acquisition has sent shockwaves throughout the global coffee industry. Costa's sale to Coca-Cola could be viewed as a direct challenge to the dominance of Starbucks in the global arena that includes the U.S. Costa has more U.K. stores than Starbucks and has been growing globally at a phenomenal rate. Add Coca-Cola's might and reach to the equation, and we may see fierce "Coffee Wars" soon. The coffee battle has just begun because of Coke's unquenched thirst for staying the number 1 beverage company in the world. Coffee-infused Coke sold all over the globe (including the United States) is almost a reality at this point.

CASE BODY

THE COCA-COLA COMPANY

The Coca-Cola Company, created in Georgia in 1886, is the world's largest beverage corporation, offering over 500 brands to consumers in 200 countries. Until the 1960s, the company offered one beverage, Coke, and aimed it at the entire soft drink market. Today, the beverage behemoth offers hundreds of products to market segments based on diverse consumer preferences for flavors, calories, and caffeine content. Although the company has diversified its product lines, Coke remains the industry leader. A sample of the different products, brands, and flavors offered by Coca-Cola in the U.S. market is shown in Table 1.

Table 1. Coca-Cola Product Portfolio

Flavor/type	**Brand Name**
Cola	Coca-Cola (Coke)
Diet/sugar-free cola	Diet Coke/Coca-Cola Light Tab Coca-Cola Zero Sugar Coca-Cola Life
Caffeine-free cola	Caffeine Free Coca-Cola
Cherry-flavored cola	Coca-Cola Cherry
"Pepper" style	Mr. Pibb Pibb Xtra
Orange	Fanta Minute Maid Simply Orange Royal Tru Orange
Lemon-lime	Sprite Lemon & Paeroa
Other citrus flavors	Mello Yello Vault Fresca Lift Lilt
Ginger ale	Seagram's Ginger Ale
Root beer	Barq's
Cream soda	Barq's Red Creme Soda
Juices	Minute Maid Fruitopia Simply Orange
Iced tea	Gold Peak Tea Fuze
Sports drinks	Powerade Aquarius Vitamin Water
Energy drinks	Full Throttle NOS Relentless Burn
Bottled water	Dasani Kinley Smartwater

Source: Coca-Cola Website (https://www.coca-colaproductfacts.com/en/products/)

In the last decade, Coke's market share has risen from 17.3% to 17.8%, while its main rival's, Pepsi, has dropped from 10.3% to 8.4%, according to trade publication *Beverage Digest*. Diet Coke and Diet Pepsi have both lost ground, but Diet Coke is still far ahead (Beverage Digest, 2019). Coke and Pepsi have fought over the past decade to win market share from one another, as overall sales dropped. As summarized in Table 2, Coca-Cola had a net revenue of $35.4 billion in 2018. That's a 15% drop in revenues from the previous year. Profits suffered as well and plummeted by a whopping $5 billion or 80%.

Table 2. Coca-Cola's Rank, Revenues, and Profits (2016-2018)

YEAR	RANK	REVENUES ($M)	PROFITS ($M)	ASSETS ($M)	EMPLOYEES
2018	87	35,410	1,248	87,896	61,800
2017	64	41,863	6,527	87,270	100,300
2016	62	44,294	7,351	90,093	123,200

Source: Fortune Magazine (www.fortune.com/fortune500/coca-cola/)

It's a tough time for carbonated soft drinks (CSD) sellers. Soft drinks sales have been in decline as soda consumption is at a 32-year low. Coke and Pepsi have both posted negative yearly sales changes for the last 15 years. And there is no salvation with the use of the word "Diet." Health experts have for years rejected the perception that diet soda is a healthy alternative. The long-term outlook is that the diet market will continue to get smaller. Today, consumers are distancing themselves not just from sugar-sweetened drinks but also artificial sweeteners themselves. Besides emerging consumers' health consciousness, Coca-Cola has also been dealing with the mounting threats of soda taxes and warning labels. San Francisco, for instance, has passed a law to add a warning label to CSD products. The label reads: "WARNING: Drinking beverages with added sugar(s) contributes to obesity, diabetes, and tooth decay. This is a message from the City and County of San Francisco" (Steinmetz, 2015). Also, when Philadelphia levied a tax on sugary drinks and soda in 2017 (1.5 cents per ounce tax), sales of those beverages fell by approximately 50% in the first year (Sorto, 2019). In brief, the two top players in beverages, Coke and Pepsi, battle for a shrinking market as customers are turning away from sugary drinks and hollow calories, and cities are imposing detrimental soda taxes.

THE COSTA ACQUISITION

Although Coca-Cola has been in business for 130-plus years and offers hundreds of products and brands to billions of customers around the globe, the company has never had a hot drink in its product mix. This changed overnight when the U.S. cola titan announced purchasing Costa Coffee on August 31, 2018, in a surprise acquisition. Coca-Cola paid a hefty £3.9 billion or $5.1 billion to purchase the British coffee company; a price that analysts argue was on the high side. Why was Coke willing to overpay to have instant access to a global coffee platform? It was because soda sales were down, and coffee consumption was on the rise (Mulier, 2018). Coca-Cola's profits had dropped from almost $9 billion in 2013 to $1.2 billion in 2018, so expanding into the more profitable and promising hot beverage industry had become more of a necessity than a luxury at that point.

The deal closed in January 2019, when European Union regulators and the Chinese government approved the acquisition. Whitbread stated it will use proceeds from the sale of the coffee business to plug a £350m pension black hole, pay off debt, return cash to shareholders, and expand its other big brand, Premier Inn hotels. Coca-Cola did not waste any time, and announced it is launching a full line of ready-to-drink (RTD) Costa products in the coming months. The global

RTD tea and coffee market size is expected to reach $135 billion by 2024, rising at a market growth of 8.4% (Arthur, 2019). Costa cold coffee and tea cans and bottles will be available wherever Coke is sold, such as at supermarkets, discount stores, vending machines, restaurants, airports, and sporting events. Although the possibilities are endless for Coca-Cola and Costa, only time will tell if Costa is a good fit. Many stakeholders are anxious to see how the acquisition turns out.

WHY COFFEE? AND WHY NOW?

That's the five-billion-dollar question! Let's start with the easier question, which is why now? Coffee is a huge business with multiple formats and categories. It is one of the fastest-growing beverage categories in the world, at 6%. Coca-Cola doesn't have a strong, global portfolio in this thriving category. CSD sales are down and coffee sales are on the rise. Coke executives had been striving to answer the question: "What areas of the beverage market do we not serve?" The unanimous answer was probably: "Coffee is a glaring hole". The number one soda maker in the world felt the urgency to diversify away from a market under increasing pressure from governments and health-conscious consumers. The timing seems perfect to get into hot beverages now. Why Costa in particular? There are a number of good reasons that made Coca-Cola lavishly spend for the deal:

- The purchase of Costa Coffee provides Coca-Cola with instant access to almost 4,000 stores in three continents. The deal also comes with a large coffee vending business of 8,000-plus Costa Express machines that are located in supermarkets, convenience stores, movie theaters, offices, and other places. Coke has virtually no experience running brick-and-mortar retail formats. Building on Costa's vast expertise and rich history is arguably the safest way to enter this unchartered territory and add a huge retail footprint overnight.

- Costa has 459 stores in China, with plans to increase its store count in the country to roughly 1,200 by 2022. The growing middle class in China is essentially driving the global economy as never before. The sheer size of the market brings a multitude of opportunities.

- Venturing into the growing RTD cold coffee with a strong global brand is another reason for the acquisition. The cola hulk already has experience in selling bottled and canned coffee in a few markets, such as Georgia coffee in Japan. The well-established Costa brand along with Coca-Cola's might and glamour could be unstoppable. Coke's distribution network is massive, and its marketing expertise and global reach add a new dimension to Costa's offerings. With Coke's 130 years of unparalleled expertise and vast distribution network, Costa could be in every supermarket, convenience store, restaurant, and vending machine that offers Coca-Cola products on the planet. This looks like a lucrative opportunity even for the largest beverage conglomerate in the world.

- Supplementing Coca-Cola's offerings in the B2B market is a possible motive for the acquisition. Currently, restaurants, hotels, and cafeterias around the world buy Coca-Cola products (CSD, energy drinks, ice tea, juices, water, etc.) to serve to patrons. Adding a well-known and prestigious coffee roaster to the mix fortifies Coca-Cola's offerings to this significant market segment and transforms the company into a total beverage conglomerate.

COCA-COLA'S EXPANSION STRATEGY

The Ansoff Matrix (Figure 1) is a marketing planning model that helps a company determine its product and market growth strategy. According to the Ansoff Matrix, there are four generic growth options: (1) Market penetration: by pushing existing products in its current market segments (i.e., increasing share); (2) Market development: by developing new markets for the existing products; (3) Product development: by developing new products for the existing markets; (4) Diversification: by developing new products for new markets. It's noteworthy that any strategy requires long-term commitment and the allocation of resources that could be irreversible, hence the importance of the decision.

Figure 1: The Ansoff Matrix

Market Penetration: Coca-Cola could pursue Market Penetration or a growth opportunity directed toward existing customers using the company's present products. Such a strategy would involve either attracting new consumers from the current target market who don't buy Coke or devising approaches that make current customers buy more. Coca-Cola could potentially increase market penetration by having its products in more stores or supplying existing stores with more CSD products and helping those stores drive greater sales through promotional activities. The argument in favor of this approach is that Coke is a market leader with massive marketing and distribution capabilities. However, in the long run, this may not be the best way to create a sustainable competitive advantage. The existing markets may become saturated and sales will drop as Pepsi increases marketing efforts and governments impose soda taxes.

Market Development: Another growth strategy is Market Development" or using the current product in new markets. This is virtually unrealistic as Coca-Cola is already in 200 countries. The soda giant is present most everywhere there is a refrigerator or a vending machine. There is little room for expansion.

Product Development: The third growth strategy, Product Development, involves developing new products that appeal to existing markets. Selling RTD coffee and tea to existing customers would be an example of a product development strategy. The value proposition is that Coke can take advantage of its existing relationships with supermarkets and grocery stores in addition to leveraging the positive attitude customers have towards the Costa brand.

Diversification**:** Diversification, the final growth strategy, would involve Coca-Cola marketing new products or services in new markets. This category can also be sub-divided into related and unrelated diversification. Related diversification is development beyond the present product market but still within the broad confines of the industry, building on existing competencies. For example, Coca-Cola opening more Costa coffee shops to serve customers outside of current markets would be related diversification. As another example, Coke could consider a complementary business, such as roasting coffee beans or selling coffee pods.

Although the Ansoff Matrix suggests that four growth strategies are possible, the two realistic options, and those that Coke is considering, are product development and related diversification. Neither market penetration nor market development advance the company toward realizing its goal of expanding away from CSD.

"COLA WARS" SPILLOVER

In the late 1800s the Coca-Cola Company (Coke) and PepsiCo (Pepsi), the world's largest cola brands, were founded in Georgia and North Carolina respectively. Since then, they have been engaged in "Cola Wars," an ultimate rivalry where the two players have come to represent much more than just two beverages. The two titans compete fiercely with each other within multiple segments of the soft drink industry all over the world. When one launches a successful product or product line extension, it's not uncommon for the other to follow with a similar competing variety of that item. The term "Cola Wars" was coined in the early 1980s to describe Coke and Pepsi's herculean sales, advertising, and marketing tactics against each other to develop and maintain market share.

Coca-Cola's competition with Pepsi is global. As with many corporations, there is frequent confrontation with competitors in nation after nation. The world's great rivalries and duopolies, for instance, Ford and Toyota, Boeing and Air Bus, Caterpillar and Komatsu, FedEx and UPS, MasterCard and Visa, and—perhaps most iconic of all—Coca-Cola and Pepsi, seem somewhat enigmatic. If a firm moves into a nation that is not currently served by its rivals, those rivals invariably follow to prevent their competitor from gaining an advantage. A few weeks before the Costa acquisition, Pepsi announced that it is purchasing the Israeli do-it-yourself carbonation company, SodaStream. The company manufactures a device that carbonates water by adding carbon dioxide from a pressurized cylinder to create soda water. SodaStream has taken advantage of the growing market for seltzer beverages and has managed to grow its customer base from 4.5 million in 2012 to 12.5 million customers. Seltzers do not have sugar and are calorie-free, hence they are healthier than the traditional soda drinks. Additionally, do-it-yourself carbonated drinks can be tailored to individual tastes with different fruits and flavors added to the water. This product appeals to consumers who are considering healthier, more environmentally friendly types of cold beverages.

Entering into the hot beverage market is very possible for Pepsi as well. After all, soda is down, and coffee is up. These two iconic companies wouldn't have thrived for 130 years if they didn't listen to their customers and gave their customers what they wanted. The beverage war continues. What will happen next?

POSSIBLE "COFFEE WAR"

Starbucks became an innovator by introducing the modern coffeehouse to American culture. It started with one store in Seattle in 1971, but it distinguished itself by a commitment to quality and as "a third place" apart from work and home. By 2018 it had more than 25,000 outlets in 75 countries. As Starbucks grew into a global coffee hulk, it inspired a generation of coffee entrepreneurs to open their own coffee shops. Starbucks has been infamous for saturating neighborhoods and tenaciously driving local coffee shops and smaller chains out of business. Many independent coffeehouses, nevertheless, have competed successfully through excellent attention to customers and providing unique beverages, atmospheres, or services to complement local tastes and preferences.

Today Starbucks is hands down the largest coffee chain in the world. Other leading chains include Dunkin Donuts (11,300 outlets), Tim Horton's (4,600 outlets), Costa Coffee (3,900 outlets), Ediya Coffee (1,500 outlets), and Doutor Coffee (1,200 outlets). It's noteworthy that McDonald's has been selling a large amount of coffee and is endeavoring to be seen as a destination for premium coffee.

To rival and outgrow Starbucks will not be a small feat for Costa. Starbucks has spread its arms around all four corners of the globe and has the first-mover advantage in many markets. The Seattle-based company is doing well in the Chinese market that it entered in 1999, with 3,600 stores in 2018, and it plans to open to a store every 15 hours to reach 6,000 stores across 230 cities by the end of 2022 (Klein, 2018). The iconic American brands Coke and Starbucks are recognized around the globe. According to rankings by the international brand consultancy firm, Interbrand (2018), Coca-Cola is the fifth most valuable brand in the world, with brand equity of $66 billion. Starbucks came in 57th with approximately $10 billion. Regardless of Starbuck's expertise and reach, Coca-Cola is likely to remain the most widely distributed American product globally as it serves two billion drinks to customers in 200 countries daily. And if Costa is to be sold where Coke is, then Starbucks has a problem on their hands.

WHAT'S NEXT?

American coffee culture has gone through several waves of acceptance. Coffee became an important part of American beverage consumption in the late nineteenth century, and James Folger started focusing his advertising on the importance of the taste of mountain-grown coffee. Demand for coffee grew consistently in the U.S., especially after World War II. This was the "First Wave" of coffee culture. In the late '60s, Alfred Peet opened a coffee shop in Berkeley, California, selling small-batch, hand-roasted coffee beans. He sold premium coffee, and the demand for his gourmet coffee grew quickly. Peet is considered the "godfather of gourmet coffee," and the demand he built can be traced to the development of Starbuck's Coffee in Seattle, which considered Peet its mentor. Peet taught the founders of Starbucks everything about gourmet coffee and even allowed them to copy his store layout and processes when they opened their first store in 1971. In the 1980s, even as coffee sales were declining, sales of specialty coffee was growing rapidly. Starbuck's rode this wave and built an empire selling gourmet coffee. This growth in the acceptance of premium-priced specialty coffee by American consumers is known as the "Second Wave." The "Third Wave" refers to the view of coffee as a culinary item. As consumer demand for craft products (notably in the brewery industry) grew, consumers began focusing on previously esoteric issues like the source of the coffee beans and the differences in flavors across different types, origins, and roasts of coffee.

The popularity of coffee in the U.S. derives from more than coffee's stimulating qualities. Its attractiveness encompasses social and cultural dimensions. Most millennials have a lifestyle that includes drinking specialty coffee and spending time at coffeehouses (reading, browsing the Internet, or socializing). Although citing the example of the millennial who spent $20,000 on coffee is an extreme case, her argument could shed some light on the significance of coffee shops in the lives of this important demographic. The young woman in the article felt no remorse spending a small fortune on her favorite beverage at coffee shops as it gave her "her security, comfort, and routine" (McClear, 2019). Coffee shops maintain a reputation as social meeting places, but depending on their location and clientele, they may also be places for study, relaxation, or to simply grab a quick snack or drink. By acquiring Costa, Coca-Cola has added a retail footprint in many parts of the world. Coca-Cola currently has 107 million fans on Facebook, making it one of the most popular brands on social media. There is no doubt Coca-Cola will bring the Costa brand to the U.S. It makes sense to expand this footprint to the biggest coffee market in the world. Retail shops are important for sales, of course, but they're also vital in building a brand, so that brand can have even more success beyond its own stores, like in direct consumption channels and home offerings. Bringing the fresh espresso-based system, Costa Express, to the U.S. opens a stream of revenue possibilities. Imagine a Costa Express next to a Coca-Cola vending machine in key places. Pushing these systems all over the country seems imminent. The company even thinks that Americans are ready for coffee infused Coke (Wiener-Bronner, 2019). However, before selling the product in the U.S., the soda giant is releasing Coca-Cola Coffee in more than 25 markets around the world by the end of 2019. Coffee-infused Coke is likely to be a reality in the United States as early of 2020.

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