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PEP Delivers Pop
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For the quarter, **PepsiCo** (PEP) beat consensus EPS estimates by a penny and revenue by a wide margin. The guidance for 2008 was in line to slightly lower than current consensus estimates. Yet, it is real funny how investors react to earnings reports and guidance.

Given what I just said and what has happened to other companies with solid results and tepid guidance, Pepsi should be getting hit, but the stock is rocketing higher. We must ask why that is the case?

I believe that we can attribute the strong response to the earnings and conference call to several factors:

- the company's ability to absorb and pass on commodity cost pressures;
- market share gains;
- growth overseas; and
- PepsiCo was an oversold consumer staple stock in an environment that favors consumer staples.

The problem is that with a \$3 plus rise in the stock, I think that any opportunity to jump into the name may have evaporated in today's action.

PepsiCo reported fourth-quarter 2007 EPS of 80 cents, excluding items, or 77 cents, including one-time items and tax benefits. Revenue for the quarter was \$12.35 billion. Excluding all one-time items, EPS grew 8% for the quarter and 13% for the full year. The company's effective tax rate rose to 27.6%, which was 220 basis points over the prior year's comparable tax rate.

In 2008, PepsiCo expects to deliver volume growth of 3% to 5%, high single-digit revenue growth and at least 10% EPS growth, which equates to at least \$3.72. (Note analysts are at EPS of \$3.74.)

PepsiCo International generated snack volume increases of 9% in the year and gained 1% of market share. Beverage volume rose 8%, with developing market growing in double digits. For the fourth quarter, snack volume was up 8%, and beverage volume was up 9%. PepsiCo International has been active acquiring snack, seed, nut and juice/beverage businesses around the world. Operating profits grew 18%. Operating margins declined 50 basis points, which was attributed to the consolidation of pre-existing joint ventures that reduced margins by 60 basis points.

Frito-Lay North America had 3% volume growth, 7% revenue growth and 7% operating profit growth in fiscal 2007. Market share grew in both volume and dollar value. The private-label business remained below 12% market share. In the fourth quarter, volume growth was 3%, revenue grew 8%, and operating profit rose 7%. Market share gains of 0.5% in volume and 0.4% in dollars were generated in the quarter. Lay's volume declined 1% in the quarter. In order to offset accelerating commodity costs, PepsiCo realized a 4% rate increase through weight reductions and price increases to consumers.

Quaker Foods had 3% volume growth, 8% revenue growth and 3% operating profit growth in the quarter.

PepsiCo Beverages North America delivered 7% revenue and 7% operating growth in 2007. The ready-to-drink tea business grew 25% in 2007 and gained significant market share. In the fourth quarter, total volume grew 1%. Carbonated soft drink volume dropped 3%, but market share rose; non-carbonated drink volume grew high single digits. Gatorade volume rose 18%.

PEP Preview: Looking for a Pop

PepsiCo (PEP) is scheduled to report fourth-quarter and full-year 2007 results before the market opens on Thursday and follow up with its quarterly conference call later that morning.

Analysts are expecting Pepsi to earn 79 cents per share on sales of \$11.56 billion for the quarter and \$3.37 per share on sales of \$41.63 billion for the full year. In the year-ago quarter, the company earned 72 cents per share on sales of \$10.38 billion.

PepsiCo has fallen roughly 17% this year and, similar to most other stocks, has broken important trendlines. This is quite surprising since Pepsi is considered a consumer staple, which tends to be a magnet for investors during times of economic weakness. Add to that the fact that Pepsi should be benefiting from a weak U.S. dollar, and we have an apparent anomaly on our hands.

PepsiCo may be falling prey to the commodity cost inflation, however, which is gripping the food and foodservices industry as a nationwide effort to increase ethanol production has taken grains and other foodstuffs out of the food chain.

Recently, I put some of my personal money (a tiny bit) into the PepsiCo dividend reinvestment plan for my charitable trust. Other than that, I currently have no plans to put client money into the name. I am closely watching, however, after its recent precipitous fall, for an opportunity to enter a company that seems to consistently grow at around 10%.

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At the time of publication, Rothbort was long PepsiCo (personal trust only), although positions can change at any time.

Scott Rothbort has over 20 years of experience in the financial services industry. In 2002, Rothbort founded LakeView Asset Management, LLC, a registered investment advisor based in Millburn, N.J., which offers customized individually managed separate accounts, including proprietary long/short strategies to its high net worth clientele.

Immediately prior to that, Rothbort worked at Merrill Lynch for 10 years, where he was instrumental in building the global equity derivative business and managed the global equity swap business from its inception. Rothbort previously held international assignments in Tokyo, Hong Kong and London while working for Morgan Stanley and County NatWest Securities.

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For more information about Scott Rothbort and LakeView Asset Management, LLC, visit the company's Web site at www.lakeviewasset.com. Scott appreciates your feedback; [click here](#) to send him an email.

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