Chapter 2
Cola Wars: Coke vs. Pepsi

Information Box
How Do We Measure the Effectiveness of Advertising?

Can a business succeed without advertising? Why or why not?

DISCUSSION POINTS: Your students will tend to think large businesses cannot, but most of them are familiar with small mom-and-pop operations that do no advertising. However, can you call these successful? But upon more reflection, some other examples of firms that do no advertising should come to mind. For example, firms that sell entirely to the government probably have little need to advertise. Likewise for firms that sell all their products to large retailers under the retailers' private brands. Many wholesalers do no advertising, instead relying on their sales reps to make the needed customer contacts. Also, small- and medium-size manufacturers selling to other manufacturers do little or no advertising, relying instead solely on sales reps. Generally your students should recognize that the primary use of a sales force does not preclude the use of some advertising. Advertising can pave the way for the sales rep by making the company and brand at least recognized. A later case in this book, Vanguard, describes a mutual fund firm that did little or no advertising for many years, but relied on word-of-mouth and publicity to build up demand.

Information Box
The Dyadic Relationship

Can you think of any situations where the dyadic theory may not work?

DISCUSSION POINTS: The dyadic relationship, which postulates that salespeople are likely to be more successful if they have characteristics similar to their customers, has been quite well tested and confirmed in various studies. Even without scientific research, most of us will agree that we usually feel more comfortable and more receptive to people with similar characteristics, backgrounds, and personalities to our own. It would seem that such rapport should carry over at executive levels as well. I have found that most students agree with this, but if some do not a more lively discussion should result.

Will the positives of dyadic relationships always work? Your students should be able to discuss this using their own experiences with salespeople. After some discussion, the general consensus will probably be that this will work only if the particular product or service is on a par with competing ones. Then the salespeople with whom you feel the most rapport will probably be preferred. But

if there are perceived differences in the products, prices, and service, then the ball game changes. Right?

What Would You Do?

Looking at Table 2.4, which shows Coca-Cola winning the war with Pepsi, at least in beverage market share, net income, and stock performance, what would you do to get PepsiCo in the growth mode, with the goal of eventually surpassing Coca-Cola in both market share and net income? Do you think PepsiCo should split the snacks and beverages company? Why or why not?

DISCUSSION POINTS: There is no easy answer to this dilemma, and if Coke stays aggressive, Pepsi may never catch up, at least in market share. With demand for soft drinks slowing, as consumers become more health conscious, and with the bulk of its business in these, the more obvious suggestion is to diversify more strongly into non-drink products, as Pepsi has long done. What other diversifications? You might want to have a brainstorming session to stimulate a variety of creative ideas.

If PepsiCo splits the snacks and beverages company, this action may take away Pepsi's advantage in diversification. On the other hand, a split may allow each of the new companies to prosper and grow on their own.

Questions

1. In the new Coke fiasco, how could Coca-Cola's marketing research have been improved? Be specific.

DISCUSSION POINTS: The marketing research involving taste tests was on treacherous ground to begin with, since most people in blind taste tests will prefer a sweeter flavor. It matters not that 200,000 people were involved in this study; the nebulosity of taste would still present difficulties in getting a definitive preference reading. Not informing participants that this new taste would be a replacement for the original flavor, and not an addition to the line, was bound to flaw the research findings since it is much easier to be supportive of a new product if the old one continues to be available. Even then, however, no taste test could uncover the depth of feeling for an old tradition, which in the case of Coke was unique in the annals of American business heritage.

Perhaps semantic differential or other attitudinal research techniques might have uncovered the depth of feeling for the old Coke. Perhaps focus group interviews, whereby small groups of consumers have a free-wheeling discussion of the topic introduced by the researcher, might have uncovered some latent resentments for such a change. Still, nothing is for certain. Marketing research is seldom a

panacea. In this situation, the media fanned the agitation, with Coca-Cola becoming a popular object of attention and criticism.

2. When a firm faces a negative press—as Coca-Cola did with the New Coke, and almost 15 years later in Europe—what recourse does the firm have? Support your conclusions.

DISCUSSION POINTS: A negative press is very difficult to combat. I doubt Coca-Cola could have done anything to counter the negative press. One would expect the publicity to die out after a few months or a year. But with such an overwhelmingly negative press and growing public sentiment, I do not believe that Coca-Cola had any other alternative but to reintroduce the old Coke.

3. "If it is not broken, don't fix it." Evaluate this statement.

DISCUSSION POINTS: The flaw in this reasoning is the belief that the environment is unchanging. It repudiates the idea of improvement and adaptation to changing circumstances. While in this case changing the flavor of the old Coke seemed to confirm the validity of this statement, in reality old Coke was steadily losing ground to Pepsi, and something needed to be done. In this case, the reintroduction of the old Coke while still keeping the New Coke turned out to be a masterstroke.

4. Do you think Coca-Cola engineered the whole scenario with the New Coke, including fanning initial protests, in order to get a bonanza of free publicity? Defend your position.

DISCUSSION POINTS: No one can say for certain that Coke did not carefully plan the whole scenario, although company officials vehemently denied this. I find it difficult to believe that any executives would have been so cunning and so tuned to future consumer reactions as to have engineered the whole thing. What do you and your students think?

5. Critique Pepsi's handling of Baesa. Could it have prevented the South American disaster? If so, how?

DISCUSSION POINTS: With hindsight it is easy to be critical of Pepsi's handling of Beach and Baesa. It should have restrained Beach's grandiose expansion plans that had caused all sorts of problems, from abysmal quality control to prodigious debt. And when an aggressive Coca-Cola counterattacked, the Baesa operation was stuck with far too much capacity. We do not know why the Pepsi executives sent to Baesa were so unable to stem the bleeding. Did they

have any authority of were they simply advisors, at least in the beginning? One suspects that Pepsi was so eager and so optimistic that this colored all judgment, until it was too late.

6. With hindsight, how might Enrico, CEO of PepsiCo, have kept Cisneros, his principal bottler in Venezuela, in the fold instead of defecting to Coke?

DISCUSSION POINTS: Since we cannot know all the details and all the nuances, we must speculate from the clues given in the case. The major clue is that Pepsi did not energetically try to maintain close ties with this bottler. The personal effort of Goizueta, CEO of Coca-Cola, on the other hand, showed graphically the importance of the human factor. Pepsi took its long-time bottler for granted, and lost him and Venezuela as a consequence. You may invite your students to discuss how specifically top executives of Pepsi could have done a better job of employing the human factor.

7. How could Coca-Cola have lessened the chances of antitrust and regulatory scrutiny in Europe?

DISCUSSION POINTS: We suspect that the critical scrutiny of Coca-Cola by European regulators was started by Pepsi's complaints that Coca-Cola was marketing too aggressively and trying to drive out smaller competitors. But Coke made other missteps that left it vulnerable to bureaucratic investigations not always unbiased. We suspect that Coca-Cola executives showed arrogance and lack of tact not uncommon among executives of other large and successful firms in their dealings with foreign officials. (We will see similar attitudes in the Disney case in Europe.) Coke initially handled the contamination scares tentatively, and this may also have set the stage for negative perceptions by foreign governments. Some students may speculate that the market dominance of Coke in some markets, such as Germany, left it particularly vulnerable, and this is a good point. It is a natural tendency for sensitive nationals to pick on a big U.S. corporation that dominates their market. But doesn't this suggest that such large U.S. firms ought to be especially careful in their dealings on foreign soils?

8. Do you think Pepsi can ever make big inroads in Coke's market share in Europe? Why or why not?

DISCUSSION POINTS: Is Pepsi likely to win the war in Europe? I think it is more likely to win the war there than in South America. The outcome of the antitrust investigations imposed some restraints on Coke amid wide publicity. The company could lose market share to Pepsi, although probably not market dominance. What do you think?

9. Do you think Coca-Cola is still a growth company? Why or why not? Defend your reasoning.

DISCUSSION POINTS: Coca-Cola's new Chairman and CEO, Muhtar Kent, certainly believes that Coca-Cola is still a growth company. He is focused on updated marketing to sell soft drinks to generate improved results. He also restored company control of North America bottling operations, giving Coca-Cola more concerted power in the market. Markets outside the U.S. may certainly offer growth opportunities. And, while not as focused as PepsiCo, Coke is attempting to appeal to health-conscious consumers. All of these actions could generate growth; however, one could argue that the soft drink industry is mature and all Coke is doing is stealing rivals' customers (especially in the U.S.). This does not suggest a strong growth company.

Hands-On Exercises

1. Assume that you are Robert Goizueta and that you are facing increased pressure in early July 1985 to abandon the New Coke and bring back the old formula. However, your latest marketing research suggests that only a small group of agitators are making all the fuss. Evaluate your options and support your recommendations to the board. (Do not be swayed by what actually happened—maybe the protests could have been contained.)

DISCUSSION POINTS: Roberto Goizueta has several options at this point. One is to abandon the new flavor and replace the old Coke. Another is to persevere with the expectation that the few agitators will get tired of it all and slacken their efforts in a few months. The last option is to reintroduce the old flavor while still keeping the new. This, of course, was the action finally taken. With marketing research showing that only a few agitators were causing all the problems and bad publicity, the temptation would have been to persevere with the expectation that the controversy would soon die down. But it might not. A few agitators, and a press eager for negative publicity about a famous product, are sufficient to bring down the mightiest of products, institutions, or persons. Not to be ignored in the decision for the third option is the advantage of having an additional product on dealer shelves, even though some dealers would likely not be well pleased. But Coca-Cola is big and the dealers can hardly prevail.

2. As a market analyst for PepsiCo, you have been asked to present recommendations to CEO Roger Enrico and the executive board, for the "invasion" of Brazil's soft-drink market. The major bottler, Baesa, is already in place and waiting for Pepsi's final plans and objectives. You

are to design a planning blueprint for the invasion, complete with an estimated timetable.

DISCUSSION POINTS: These recommendations for invading Brazil's soft-drink market can be as detailed and specific as you think time permits. For a very specific exercise, you may want to form the class into groups, and perhaps have a homework assignment to come up with detailed plans and a timetable, given that the major bottler is already in place. Otherwise, you can have an informal class discussion with no particular preparation. In either case, you should expect your students to propose a more carefully controlled and better research expansion than was actually done. But don't let them get away with mere platitudes and generalities. Pin them down. How do they propose to institute better controls, and what kinds of controls would these be? How are they going to research the expansion and the market potential? Any contingency plans?

3. You are a staff assistant to Ivester. It is 1998, and he has just assumed the top executive job with Coca-Cola. One of his first major decisions concerns raising soft-drink prices over seven percent to improve operating margins and make up for diminished revenues in a depressed European market. He wants you to provide pro and con information on this important decision.

DISCUSSION POINTS: As a staff assistant to Ivester and charged to provide pro and con information on raising soft-drink prices 7.6% to improve operating margins, you will need to provide at least the following considerations, and even weight their impact:

For raising prices:

- profit margins will be nicely increased, and this should result in increased profitability even if revenues suffer slightly.
- while revenues may suffer a little in a depressed European market, this should be temporary. After all, how can a 7% increase in a soft drink affect adversely any family's budget. It certainly should not in the North American market.
- If we are a price leader in this, our competitors most likely will eagerly follow suit.

Against this price rise:

- In a depressed European market, what is raising prices going to do to demand? At best, maybe not very much, but how about the worst scenario: drastically affecting revenues, and even giving market share to competitors.
- Aren't there other things we can do to help profits? Have we exhausted all possibilities for increasing sales?

Of course, no one could predict the contamination scare that occurred not many months later in Europe. Perhaps more surprising was the negative effect on sales in North America.

Team Debate Exercises

We have tested the debate format in classrooms and it has generated a lot of student interest in persuasively presenting controversial positions, defending them, and attacking opposing viewpoints. We have found that most students, once they get the feel for adversarial confrontations—common in law schools, rather uncommon in business schools—eagerly adapt to their roles. In the process, they learn skills that can have strong career benefits. Such debates seem best used when students, in two groups of three or four, are given several days to formulate their positions with each member of the group involved in some part of the oral presentation.

1. Debate the issue of whether Coke is in a mature stage of the life cycle or whether it is still in a growth stage. In the course of debate, each side should consider how best to maximize its performance.

DISCUSSION POINTS: This debate should consider the characteristics of growth and maturity product life cycle stages. A company in a growth stage typically faces rapidly rising sales, rising profits, and a growing number of competitors. Early adopters join innovators as customers. A company in a mature stage typically faces peak sales, high profits, and a stable or slightly declining number of competitors. The middle majority become customers.

2. Debate Ivester's plan to distribute millions of free bottles of Coke products to people in Belgium and Poland. In particular, debate the costs versus benefits of this recovery strategy. Are the benefits likely to be worth the substantial cost?

DISCUSSION POINTS: The belated plan of Ivester to distribute millions of Coke products to Belgium and Poland should arouse strong opinion differences, if your students consider the costs of such a plan. The debate, of course, would separate those who agree with such an aggressive approach to win back customers versus those who maintain this is overkill, and not by any means worth the cost. You may want to have your students make some assumptions on the costs of such a remedial effort, and this is fine, but they should identify the rationale for their assumptions, and come up with some specifics. For the group that proposes less drastic actions, let them also be specific about their alternative proposal. And have a good debate.

3. Debate the issue of Coca-Cola diversifying into non-drink products, such as Pepsi had done quite successfully.

DISCUSSION POINTS: The issue essentially is whether to concentrate resources or to dilute them. Some of the questions to be raised in the debate are whether Coca-Cola has the managerial resources to effectively handle such diversifications. It has taken Pepsi some years to establish itself in this highly competitive market. How are these non-drink diversifications going to affect profit margins? Probably negatively. How necessary are such diversifications to growth?