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From Soda to Coffee: Analyzing Coca-Cola's Acquisition of Costa Coffee

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Abstract

As the carbonated soft drink industry faced declining consumption in Western markets from the early 2000s, even industry leaders like Coca-Cola were affected. Coca-Cola made a significant strategic change to revive its growth by acquiring the coffee house chain Costa Coffee. This acquisition marked an expansion from its traditional core market of carbonated soft drinks into the coffee industry. The following thesis explores Coca-Cola's challenges, motives behind this acquisition, and potential benefits and risks. Furthermore, Costa Coffee's growth strategy after its acquisition by Coca-Cola is examined.

This thesis uses a pedagogical case approach. It includes a review of academic literature on growth strategies based on the Ansoff Matrix, inorganic growth approaches, and the business environment. This is followed by the description of the case. Finally, teaching notes are provided to guide the application of the case in classes related to corporate strategy and acquisitions.

The findings show how Coca-Cola was pressured by changing consumer preferences and the evolving legislation to expand beyond its traditional product portfolio. This led the company to its new strategic goal of becoming a "total beverage company." As part of its transformation, Coca-Cola announced the acquisition of Costa Coffee in 2018. The acquisition allowed Coca-Cola to enter the growing coffee market and leverage its strengths in ready-to-drink products. After being acquired, Costa Coffee's strategy focused on expanding internationally, exploring new distribution channels, and introducing new products.

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Abstract

À medida que o consumo de refrigerantes carbonatados declinava nos mercados ocidentais desde o início dos anos 2000, até líderes do setor, como a Coca-Cola, foram afetados. Para impulsionar o seu crescimento, a empresa adotou uma mudança estratégica significativa ao adquirir a rede de cafeterias Costa Coffee. Esta aquisição marcou uma expansão do seu mercado tradicional de refrigerantes, para a indústria do café. Esta dissertação analisa os desafios da Coca-Cola, os motivos desta aquisição e os seus potenciais benefícios e riscos. Para além disso, também será analisada a estratégia de crescimento da Costa Coffee após a sua incorporação na Coca-Cola.

Esta tese segue a abordagem de um caso pedagógico. Inicialmente inclui uma revisão da literatura académica sobre estratégias de crescimento com base na Matriz Ansoff, nas alternativas de crescimento inorgânico e no ambiente de negócios. Em seguida, descreve-se o caso e, por fim, fornecem-se notas de ensino para a sua aplicação em aulas sobre estratégia corporativa e aquisições.

Os resultados mostram que a Coca-Cola sentiu a pressão das mudanças nos hábitos dos consumidores e das novas regulamentações, o que a levou a diversificar o seu portfólio. O novo objetivo era tornar-se uma “total beverage company”. A compra da Costa Coffee foi um passo fundamental nessa transformação, permitindo à Coca-Cola entrar num mercado em expansão e aproveitar a sua experiência em bebidas prontas para consumo. Após a aquisição, a Costa Coffee apostou na expansão internacional, na diversificação dos seus canais de venda e no lançamento de novos produtos.

Título: Do refrigerante para o café: Análise da aquisição da Costa Coffee pela Coca-Cola

Autor: Jan Eichhorn

Palavras-chave: Crescimento Empresarial, Estratégias de Crescimento, Matriz de Ansoff, Fusões e Aquisições, Ambiente de Negócios, Bens de Consumo

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List of Abbreviations

bn	Billion
CEO	Chief Executive Officer
COVID-19	Coronavirus disease 2019
Costa	Costa Coffee
CSD	Carbonated Soft Drinks
EBITDA	Earnings Before Interest, Taxes, Depreciation, and Amortization
GBP	British Pounds
GDP	Gross Domestic Product
m	Million
NRTD	Not-Ready-to-Drink
OOH	Out-of-Home
RTD	Ready-to-Drink
S&P 500	Standard & Poor's 500
UK	United Kingdom
US	United States
USD	US-Dollars

1. Introduction

Revenue growth is a fundamental objective for any company, yet it remains challenging to achieve (Bradley et al., 2022). A quarter of all companies are not growing at all on a yearly

basis. Even among Standard & Poor's 500 (S&P 500) companies, only one in ten has consistently shown annual growth above gross domestic product (GDP) for more than three decades (Birshan et al., 2022). To ensure long-term growth, companies are increasingly exploring new growth opportunities (Birshan et al., 2022). Business leaders expect 50% of their revenues to be generated through new products or services within the next five years (Birshan et al., 2022). Particularly in the consumer goods sector, where rapid growth is rare, expanding into new categories through innovation or acquisition is a critical strategic focus (Bar Am et al., 2022).

Coca-Cola's purchase of the coffee house chain Costa Coffee (Costa), announced in 2018, is a compelling example of exploring new growth opportunities through an acquisition. Coca-Cola faced challenges in its core carbonated soft drinks (CSD) market, such as health concerns about its products. This has led Coca-Cola to enter the emerging global coffee market (Montgomery & Weber, 2021). The acquisition marked Coca-Cola's first involvement in the hot beverages market and introduced the difficulty of operating a retail business on a global scale. One European investment banker described the acquisition as a transformative step for Coca-Cola: "In many ways you could argue that this is the biggest strategic shift made by [Coca-Cola] in its history." (Gray & Fontanella-Khan, 2018, para. 17).

This thesis explores Coca-Cola's challenges, the acquisition's motives, and potential benefits as well as risks. Additionally, it examines Costa Coffee's post-acquisition growth strategy.

After the introduction, the thesis describes the theoretical background of corporate growth, growth strategies, inorganic growth approaches, and the business environment. Next, the methodology and the rationale for the case selection are explained. The following part includes the case, outlining both companies' pre- and post-acquisition development. Thereafter, the pedagogical use and the analysis of the case are discussed. In the end, the thesis presents limitations and concludes with a summary of the key findings.

2. Literature Review

1.

2.

2.1 Fundamentals of Corporate Growth

Penrose (1959) introduced the classical theory of corporate growth, viewing it as a process of resource accumulation and strategic decision-making. She considers companies an accumulation of resources and argues that underutilized resources are key to corporate growth (Penrose, 1959). Therefore, the ability of managers to identify growth opportunities and utilize underused resources is essential for driving corporate growth (Penrose, 1959).

Corporate growth can be measured in various ways, including sales, employment, assets, market share, and profits (Zhou & De Wit, 2009). Sales and employment are easily accessible, reflect both short-and long-term effects, and are therefore the most widely used indicators for corporate growth (Zhou & De Wit, 2009). A firm can grow organically, e.g., by developing products, inorganically, e.g., by acquiring companies, or by combining both methods, e.g., franchising (McKelvie & Wiklund, 2010).

Corporate growth enables companies to attract talent, access new financial resources, and prevent competitors from replacing them (Canals, 2001). Growing firms can attract talent more easily, as employees expect better career opportunities in such companies (Goold, 1999). Furthermore, corporate growth draws financial resources since fast-growing companies receive higher valuations, while slower-growing companies are viewed as less attractive investments (Goold, 1999). In addition, finding new ways for a company to grow reduces the threat of competitors imitating or replacing its offerings (Canals, 2001).

Despite the benefits of corporate growth, excessive growth can cause problems (Raisch & von Krogh, 2007). It can, for example, overwhelm management capabilities by increasing organizational complexity, resulting in a loss of control (Raisch & von Krogh, 2007).

2.2 Corporate Growth Strategies: The Ansoff Matrix

A company can pursue various growth strategies, as illustrated in the Ansoff Matrix (Figure 1) (Ansoff, 1957). This framework classifies growth strategies into different approaches based on their product-market strategy (Ansoff, 1957). Markets refer to customers, while products are defined as items or services sold to customers (Lynch, 2011).

The strategies outlined in the Ansoff Matrix include 1) market penetration, 2) market development, 3) product development and 4) diversification (Ansoff, 1965). These strategies are not mutually exclusive, as companies often pursue several strategies simultaneously (Ansoff, 1957).

		Products	
		Existing	New
Markets	Existing	Market Penetration	Product Development
	New	Market Development	Diversification

Figure 1: Ansoff Matrix (Ansoff, 1965)

Market penetration focuses on increasing sales by selling existing products within the current markets (Lynch, 2011). The strategy aims to encourage customers to buy more frequently and to purchase more products in each transaction (Kotler, 2003). This can be accomplished by promoting or repositioning products (Hussain et al., 2013). Market penetration is easier to achieve in a less mature market, where customer loyalty is lower. This environment facilitates attracting new customers from competitors (Lynch, 2011).

Market development refers to entering new markets with existing products, which may be slightly modified (Ansoff, 1957). It intends to increase sales by accessing new customers and converting non-users into customers (Kumar, 2016). Achieving market development includes attracting a new customer segment, entering new geographical regions, or identifying new uses for existing products (Lynch, 2011).

Product development encompasses introducing new products to existing markets (Ansoff, 1957). It includes substantial product advancements rather than minor modifications (Lynch, 2011). An essential aspect of product development is innovation. Therefore, management's inability to implement innovation strategies poses a barrier to this strategy (Crawford, 1972). In addition, product development needs to be aligned with the overall business goals to succeed (Cooper & Edgett, 2010).

Diversification means entering new markets with new products (Ansoff, 1957). It requires organizational and physical changes within the company (Ansoff, 1957). Unlike the other strategies that primarily leverage existing resources, diversification is often associated with new skills, techniques, or facilities (Ansoff, 1957). It often leads to a simultaneous exit from the existing product-market strategy (Ansoff, 1957). Its success depends on management's capability to manage an unrelated business (Cyriac et al., 2012). As this task is challenging for managers (Cyriac et al., 2012), the diversification strategy is considered the riskiest option among the outlined strategies (Lynch, 2011).

2.3 Inorganic Growth Strategies: Strategic Alliances, Mergers and Acquisitions

Inorganic growth, encompassing strategic alliances and mergers and acquisitions, has become increasingly relevant for many companies (Hoffmann & Schaper-Rinkel, 2001). A strategic alliance is a collaboration between two or more companies that works towards strategic goals that benefit all companies involved (Hunger & Wheelen, 2000). While mergers and acquisitions are often understood synonymously, they differ in their implications. A merger combines at least two firms to create a new legal entity, while an acquisition describes one company gaining control of more than 50% of the target company (Singh, 1971). For simplicity, the term "acquisition" will be used to refer to both mergers and acquisitions.

Despite their growing relevance, inorganic growth strategies often fail (King et al., 2004; Lavie & Miller, 2008), as companies frequently make the wrong strategic decision. Reasons for this are the reliance on experience and organizational inefficiencies (Dyer et al., 2004). Companies, for example, that engaged in successful alliances are inclined to pursue another alliance without considering an acquisition (Dyer et al., 2004). Furthermore, the teams responsible for alliances and acquisitions often work in silos and report to different executives, which hinders the company from evaluating both options (Dyer et al., 2004).

Motives for a strategic alliance include market expansion, resource and skill acquisition, and product development (Varadarajan & Cunningham, 1995). For example, an alliance eases entering new markets, as a company benefits from the expertise of a regional alliance partner (Varadarajan & Cunningham, 1995). Furthermore, alliances facilitate product development by distributing the associated financial risk across several companies (Hunger & Wheelen, 2000).

Several factors, such as cultural differences and lack of trust, contribute to the failure of an alliance. The culture greatly influences day-to-day work and can lead to problems if cultural differences are not addressed in an alliance (Das & Kumar, 2010). The absence of trust is particularly problematic when an alliance faces struggles. Then, strategic partners often blame each other and leave unsolved problems (Elmuti & Kathawala, 2001). Other risks of strategic alliances include unclear objectives and poor coordination between the companies (Elmuti & Kathawala, 2001).

While strategic alliances are generally less risky, some companies choose a more uncertain approach through acquisitions (Dyer et al., 2004). The low success rate of acquisitions (Hitt et al., 2009) raises the question of why companies pursue them. The motives of acquisitions can be grouped into four categories: value creation, managerial self-interest, environmental factors, and firm characteristics (Haleblian et al., 2009).

A key driver of acquisitions is value creation, as companies seek to increase their market power or achieve efficiencies through synergies (Haleblian et al., 2009). Market power theory suggests that companies, by acquiring competitors, reduce the competition and thereby gain the power to charge higher prices (Kim & Singal, 1993). Synergies can result from the better allocation of resources within the new company, such as replacing inefficient management with more efficient management (Piesse et al., 2022).

Acquisitions are driven not only by value creation but also by managerial self-interest (Haleblian et al., 2009). Managers may pursue acquisitions to increase their monetary compensation (Haleblian et al., 2009) or their power by managing larger firms (Gomez-Mejia & Wiseman, 1997). Moreover, overconfident managers overestimate their ability to create value through acquisitions, resulting in an overpayment of the target firm and hence value destruction for the acquirer (Malmendier & Tate, 2008; Roll, 1986).

Environmental factors, such as regulatory changes, also influence acquisition decisions (Haleblian et al., 2009). Companies unable to adapt their strategies to their environment are more likely to engage in acquisitions (Thornton, 2001). Furthermore, acquisitions can be sociologically motivated as firms tend to imitate companies that have been successful in making acquisitions or companies they are connected with (Haunschild, 1993; Stearns & Allan, 1996).

Finally, firm-specific characteristics are important for understanding the antecedents of acquisitions, as a firm's acquisition experience, strategy, or position in the market affects its acquisition behavior (Haleblian et al., 2009).

An acquisition is divided into a pre-acquisition phase, involving strategic planning and target selection, and a post-acquisition phase, focusing on integration and alignment (Gomes et al., 2013). Both phases are separated by the closing date, when the ownership is transferred from one company to another (Gomes et al., 2013).

Success factors in the pre-acquisition phase include choosing the right company, having a clear strategy, and paying an appropriate price (Gomes et al., 2013). The target selection should be based on the strategic and organizational fit (Angwin, 2001). Strategic fit refers, for example, to resource similarity and complementarity between the acquirer and the acquisition, while organizational fit includes, for example, cultural differences. If the acquisition fits strategically and organizationally to the acquirer, the likelihood of acquisition success is higher (Gomes et al., 2013). Furthermore, acquisitions are more successful when the acquirer has an acquisition strategy and prior experience with acquisitions (Barkema & Schijven, 2008). In contrast, paying too much for the acquisition destroys value for the acquirer by making it challenging to generate a sufficient return on the investment (Goold et al., 1994).

Once the acquisition is completed, the post-acquisition phase begins. Critical factors in this phase are leadership, communication, and the integration strategy (Gomes et al., 2013). Insufficient leadership, such as unclear decisions and weak management skills, can lead to acquisition failure (Angwin & Meadows, 2009). Therefore, leadership should act proactively and set clear goals that align with the company's overarching strategy (Hyde & Paterson, 2002). In addition, communication is essential to convey integration plans and mitigate stakeholders' fears (Schweiger & DeNisi, 1991).

Furthermore, the acquirer's integration strategy is crucial for the acquisition's success (Gomes et al., 2013). While the acquirer needs to integrate acquisitions to realize synergies (Puranam et al., 2003), excessive integration can lead to employee turnover or loss of autonomy for the acquisition (Puranam et al., 2003). Integration approaches can be categorized into five strategies based on two dimensions: 1) the autonomy retained by the acquisition and 2) the extent of knowledge transfer through shared assets, personnel, or information between the companies (Figure 2) (Angwin & Meadows, 2015). The identified integration strategies are:

- 1) Preservation – Retaining the acquired firm’s culture and practices (Haspeslagh & Jemison, 1991);
- 2) Symbiosis – Keeping core elements of the acquisition while continuously integrating the acquisition in a collaborative process (Haspeslagh & Jemison, 1991);
- 3) Absorption – Integrating valuable assets of the acquisition while non-valuable assets are divested (Haspeslagh & Jemison, 1991);
- 4) Intensive Care – Restructuring of the acquisition through financial controls and centralized strategy (Angwin & Meadows, 2015);
- 5) Reorientation – Partial integration of central functions, such as human resources or marketing, but no significant adjustments to operations (Angwin & Meadows, 2015).

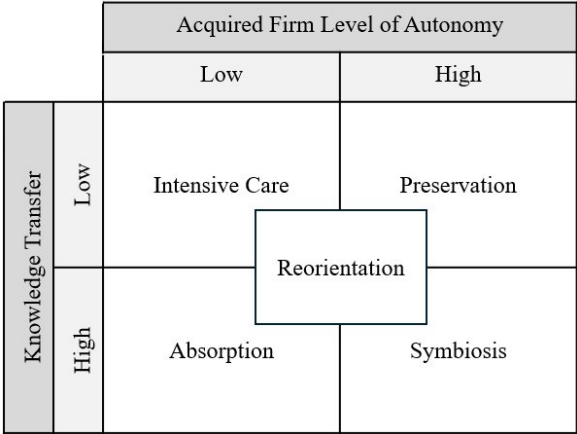


Figure 2: Post-Acquisition Integration Strategies (Angwin & Meadows, 2015)

2.4 Business Environment and PESTEL Analysis

A company's growth is shaped not only by internal decisions but also by its business environment, which influences key aspects like strategy formulation (Bourgeois, 1980; Kotha & Nair,

1995). To successfully compete, the firm's strategy must be aligned with its business environment (Donaldson, 2001).

The business environment is separated into the macro-environment, which influences an entire industry, and the micro-environment, which refers to company-specific factors (Carruthers, 2009; Itani & Mason, 2014). While the macro-environment encompasses broader societal influences such as political factors, the micro-environment includes, for example, competitors (Cherunilam, 2009).

To react more adequately to environmental developments, environmental scanning was introduced (Aguilar, 1967). This process aims to identify, collect, and translate information about the company's environment to assist top management (Aguilar, 1967). The intensity of environmental scanning differs from company to company. It can range from unstructured data collection to systematically screening the environment (Jain, 1984). Environmental scanning helps companies to anticipate changes, identify strategic threats and opportunities and monitor competitor activities (Babatunde & Adebisi, 2012).

A tool for scanning the macro-environment is the PESTEL analysis (Hunger & Wheelen, 2000), which encompasses 1) political, 2) economic, 3) social-cultural, 4) technological, 5) environmental, and 6) legal factors (Worthington & Britton, 2006).

The political environment includes factors such as the political system or government involvement in the economy (Worthington & Britton, 2006). For example, establishing the European Union has led to an increase in international acquisitions (Hunger & Wheelen, 2000).

The economic environment covers factors such as GDP growth rates, inflation, or interest rates (Cherunilam, 2009). Economic factors have a direct effect on a company's business. For instance, higher interest rates often lead to decreased demand for real estate due to increased borrowing costs (Hunger & Wheelen, 2000).

The social-cultural environment encompasses customer trends, habits, and population characteristics (Babatunde & Adebisi, 2012). An aging population, for instance, leads to a smaller workforce, which could result in higher labor costs for the company (Babatunde & Adebisi, 2012).

The technological environment includes factors such as research activity and rate of technological change (Babatunde & Adebisi, 2012). For example, improvement in computer microprocessors led to the widespread adoption of home computers (Hunger & Wheelen, 2000).

Environmental factors such as the availability of natural resources and weather conditions have gained importance in recent years (Cherunilam, 2009). An example is freshwater, which is becoming scarce in certain regions due to droughts (Hunger & Wheelen, 2000).

The legal environment refers to laws that regulate business operations, such as laws that govern the company's customer relationships (Worthington & Britton, 2006).

3. Methodology & Case Selection

This study uses a qualitative approach to examine Coca-Cola's acquisition of Costa. Multiple sources were used to provide a comprehensive case. The case contains information from corporate documents, industry reports, case studies, and press articles. The various corporate documents give insights into the companies' business models and financial performances. Moreover, industry reports and case studies provide information about the competitive landscape that the companies were exposed to. Lastly, the press articles describe miscellaneous topics around the acquisition, such as regulatory changes, evolving consumer preferences or analysts' insights.

The case of Coca-Cola's acquisition of Costa was selected due to its topicality and strategic relevance. The case is particularly intriguing because Coca-Cola did not have any retail experience. Hence, the distinct business models of the companies, one being a consumer goods company and the other a retailer, provide an interesting opportunity to discuss how synergies can be exploited. In addition, both companies operate globally and play a significant role in their respective industries, providing a rich basis for analyzing the acquisition's challenges and opportunities. Finally, the companies' business models are characterized by their simplicity, enabling the reader to focus on analyzing the teaching questions.

4. Teaching Case

3.

4.

4.1 Coca-Cola's Strategic Move into the Coffee Market

In August 2018, Coca-Cola announced a move that few anticipated: the acquisition of the coffee house chain Costa for \$5.1 billion (bn) (Coca-Cola, 2018b). This marked Coca-Cola's largest acquisition in eight years (Gray, 2018).

After decades of success built on soda, the Atlanta-based beverage giant found itself at a critical point. CSD consumption in key markets like the United States (US) was declining (Montgomery & Weber, 2021). Growing concerns over sugary drinks, moved Coca-Cola's chief executive officer (CEO) James Quincey to set a new goal in 2017: to transform Coca-Cola into a "total beverage company" that sells a broad range of products such as water, tea, or coffee (Coca-Cola, n.d.-b, para. 1; Gray & Fontanella-Khan, 2018). At the time, coffee was among the fastest-growing beverage categories and presented Coca-Cola with a promising opportunity for expansion. (Ahmed et al., 2018). Consequently, Coca-Cola acquired Costa and made its first entry into the hot beverage market (Selwood & Mattinson, 2018).

However, not all reactions to Coca-Cola's entry into the coffee market were positive. Analysts of the Swiss bank UBS argued that Coca-Cola had overpaid Costa, noting that Coca-Cola paid a multiple of 16.4 times Costa's 2018 Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA) (Selwood & Mattinson, 2018). In comparison, the enterprise value of Starbucks, the world's largest coffee house chain, was valued at a multiple of 13 times EBITDA (Selwood & Mattinson, 2018). Analysts were also concerned about Coca-Cola's lack of retail experience and its ability to manage a coffee chain with 3,800 stores. Moreover, Coca-Cola significantly increased its headcount from approximately 60,000 to 80,000 through this acquisition, thereby adding complexity to its organizational structure (Gray & Fontanella-Khan, 2018).

While James Quincey acknowledged the complexities of this acquisition, he reassured stakeholders that Coca-Cola would take over Costa's management team to retain expertise and ensure a smooth transition (Gray & Fontanella-Khan, 2018).

4.2 Coca-Cola's Recent Developments: Expanding with Strategic Acquisitions

After successful years in the 20th century, the CSD industry faced challenges when per-capita soda consumption in the US began declining in the early 2000s (Montgomery & Weber, 2021). This has led to an industry-wide decline from 10,377 million (m) CSD products sold in 2004 to 8,520m in 2014 in the US (Montgomery & Weber, 2021).

In response to these challenges, Coca-Cola began to grow outside of the CSD market by acquiring the vitamin water company Glaceau (Berk, 2007), the iced tea company HonestTea (Coca-Cola, 2011), and the smoothie company Innocent (Lucas, 2013). However, not all these ventures were successful, as Coca-Cola discontinued the once-acquired HonestTea (Coca-Cola, 2022). Also, Coca-Cola already had its first contact with the coffee industry through a collaboration with the coffee machine company Keurig Green Mountain in 2014 (Taylor, 2014). The companies launched a brewing machine for soft drinks, which failed as the so-called "Keurig Kold" was stopped within a year after its launch (Zhang & Taylor, 2016).

In 2018, the year the acquisition of Costa was made public, Coca-Cola had generated revenues of \$31.9bn (Appendix A) (Coca-Cola, 2018a). In 2018, 70% of its units sold came from sparkling soft drinks, while only 4% came from the category "tea and coffee" (Appendix B). Despite its comprehensive product portfolio, Coca-Cola lacked a global coffee brand (Coca-Cola, 2018a). It only operated regional coffee brands focused on ready-to-drink (RTD) products. RTD products are beverages that are ready to consume without additional preparation (Statista, n.d.-b). The most significant of Coca-Cola's RTD coffee brands was Georgia Coffee, available in Asian countries with a strong focus on Japan (Lucas, 2019). CEO James Quincey acknowledged when Costa's acquisition was announced: "Hot beverages is one of the few segments of the total beverage landscape where Coca-Cola does not have a global brand." (Coca-Cola, 2018b, para. 6).

4.3 Growing Challenges in the CSD Market

One reason for growing pressure on Coca-Cola was rising health concerns among customers. Between 1975 and 2016, the global adult obesity rate increased from 21% to 39% (Coppola, 2023), leading customers to reassess their nutrition and turn away from high-sugar products (Raphelson, 2018). As a result, demand for CSD declined in Europe and North America (BBC, 2016; Montgomery & Weber, 2021). In 2013, Indra Nooyi, then-CEO of Coca-Cola's long-time rival Pepsi, already stated concerns about consumers shifting away from CSDs: "We actually believe that if you let this go too long, another three or five years, the consumer will walk away from carbonated soft drinks." (Montgomery & Weber, 2021, p. 4).

Due to the health concerns, Coca-Cola faced criticism for its role in the unhealthy consumption of its drinks, with Forbes journalist Hank Cardello commenting: "To be a true industry leader, the company must step up and own the problems the industry has helped create." (Cardello, 2019, para. 7).

Along with health concerns, more people started switching from Coca-Cola to coffee for caffeine intake. While CSD used to outsell coffee by a three-to-one relation in the US, analysts predicted that coffee consumption would surpass CSD by the 2020s (Raphelson, 2018). Simultaneously to the shift towards coffee, there has been a shift in taste preferences in CSD with younger consumers showing growing interest in unique flavors (Dye, 2018). In response to these trends, Coca-Cola aimed for product innovation and introduced 500 new products in 2017 alone (Coca-Cola, 2017).

Also, the regulatory landscape of the beverage industry evolved before the acquisition of Costa. Over 50 countries, including the United Kingdom (UK) and France, implemented sugar taxes to promote healthier products and discourage users from unhealthy nutrition (Obesity Evidence Hub, 2024). While no national sugar tax existed in the US, more than 40 counties and seven cities had taken action by 2018 (Belluz, 2018). For example, Philadelphia's tax on sweetened beverages led to a 38% decrease in adjusted sales of taxed drinks in Philadelphia (McCrystal, 2019).

4.4 Coca-Cola's Strategic Shift to a "Total Beverage Company"

The necessary change within Coca-Cola came with James Quincey, who became CEO of the company in 2017 (Coca-Cola, n.d.-a). Quincey aimed to transform Coca-Cola both commercially and culturally. He broke the traditionally formal dress code of Coca-Cola and showed up in jeans at town hall meetings. This move impressed the employees and highlighted his intention to create a new company spirit, as Quincey noted: "The message was that it was time to turn the page." (Montgomery & Weber, 2021, p.6) .

Moreover, Quincey wanted to establish a growth mindset within the workforce. Therefore, he wanted to move away from a tenure-oriented culture and instead focus on a performance- and team-oriented culture by increasing the proportion of performance-based payments (Montgomery & Weber, 2021).

A central goal for Quincey was to make Coca-Cola more customer-centric. To achieve this, he saw the need to expand the product portfolio and become more risk-taking with smaller brands (Maloney, 2017). As part of this change, he implemented more agile structures within the company. Quincey reduced Coca-Cola's Atlanta headquarters staff by 1,200 (Thomas, 2017) and shifted more power to the geographic operating groups (Montgomery & Weber, 2021).

In May 2017, Quincey unveiled his vision to transform Coca-Cola into a "total beverage company" (Coca-Cola, n.d.-b, para. 1). Coca-Cola's CEO aimed to shift the company beyond CSD and offer a wide range of drinks, from water and juices to energy drinks and coffees. While he acknowledged the evolving consumer preferences, he wanted to focus more on low- and no-sugar beverages and beverages in emerging categories (Montgomery & Weber, 2021). Quincey explained that inorganic growth will also be an essential part of the expansion strategy: "We absolutely see the likely trajectory is accelerating our own innovation and scaling brands that are working, such as smartwater or Honest Tea, but also continuing to invest in smaller companies and make acquisitions to bring more billion-dollar brands into the pipeline." (Quincey, 2017, p.6).

4.5 Costa's Rise to a Market Leader

After being acquired by Whitbread in 1995, Costa expanded rapidly and became the second largest coffee house chain by number of stores worldwide (more than 3,800 coffee shops in

2018) and the largest in the UK (Appendix C) (Ahmed & Pooley, 2018; BBC, 2018; Eley, 2018a). It was not only the largest but also the most liked chain in the UK (Whitbread, 2017a).

Costa has pursued a multi-channel strategy to secure its leading position in the UK coffee market. The strategy included operating equity stores (stores fully owned by Costa), franchises, and the “Costa Express” self-service vending machines (Whitbread, 2017a). In 2018, Costa reported revenues of £1,292m (\$1,718m*), of which £1,131m (\$1,504*) came from its home market in the UK, while it generated £161m (\$214m*) internationally (Whitbread, 2018).

In 2018, the coffee company operated over 2,400 coffee shops in the UK and over 1,400 coffee shops abroad in more than 30 countries (Ahmed & Pooley, 2018). Over 450 international shops were located in China (Green, 2018). China was a key market for Costa’s international expansion due to its growing coffee culture and the high reputation of Western brands in the Chinese society (Rovnick, 2017; Whitbread, 2017a).

Costa’s success was, among other things, driven by its innovative customer strategies, such as the loyalty program “Costa Club” (Whitbread, 2018). This program had over 5m active users in the UK and accounted for more than 40% of all transactions in the UK in 2018 (Whitbread, 2018). Moreover, the company has introduced digital services like “Costa Collect,” an app to pre-order drinks and food, and experimented with concept stores such as Costa Pronto, a high-speed store for busy customers (Whitbread, 2017a).

A cornerstone of Costa’s growth strategy was its expertise in sourcing and roasting coffee (Collis & Wert, 2023). In 2017, the company opened a new roastery, quadrupling Costa’s roasting capacities. Dominic Paul, then managing director of Costa at the time, viewed this as a key part of the company’s strategy:

Turning on our new roasting capacity is a landmark for the business. It’s a statement of our ambition to grow and our passion for great coffee. (Whitbread, 2017b, para.7)

* See Appendix D for conversion rates

4.6 Costa's Performance and Challenges Prior to the Sale

Before its sale to Coca-Cola, Costa and its parent company Whitbread drew significant media attention due to its recent performance. Despite its revenue growth from £1,202m (\$1,550m*) in 2017 to £1,292m (\$1,718m*) in 2018 (Whitbread, 2018), the like-for-like sales (sales from the same stores over a specific period, excluding new openings or closures) development was concerning. In the first half of 2017, like-for-like sales increased by only 0.6% compared to 4.4% in the same period of 2015 (Appendix E) (Ahmed, 2017b). The decreased growth was primarily driven by the intense competition from larger rivals such as Starbucks and the rise of artisan cafes (Ahmed, 2017b).

In addition to the competitive pressure, UK consumers reduced their overall consumption compared to previous years (Ahmed, 2017a). This effect was further reinforced by Costa's choice of locations for its coffee shops. With 60% of its shops located in shopping centers or retail parks, the company was particularly vulnerable to reduced footfall in these areas, as indicated by consumer behavior (Eley, 2018a). On the cost side, higher barista wages and rising import costs for coffee beans negatively impacted Costa's performance (Ahmed, 2017b). These factors have resulted in Costa's statutory profits falling from £130m (\$168m*) in 2017 to £123m (\$164m*) in 2018 (Whitbread, 2018).

Another reason for Costa's high media presence was the emergence of activist investors. First, the US-based hedge fund Sachen Head bought around 3.4% of Whitbread's shares in December 2017 (Pooley, 2018). Half a year later, Elliot Advisors, also a hedge fund company, bought 6% of Whitbread (Eley, 2018b). At the time, both hedge fund companies aimed for a spin-off of Costa (Pooley, 2018). By doing so, the investors hoped that Costa's shares would be re-evaluated at a higher price. In April 2018, after constant pressure from the investors, Whitbread agreed to spin-off Costa (Eley, 2018c).

4.7 Global Coffee Market: An Emerging Opportunity

The global coffee market emerged as one of the fastest-growing consumer goods categories in 2018 (Appendix F) (Ahmed et al., 2018). Over the past two decades, global coffee consumption has increased by 60%. (ICO, 2018). Emerging markets in South-East Asia primarily drove this growth, as the coffee consumption in China for example grew on average at 12% annually

from the early 1990s until 2017 (Appendix G) (ICO, 2018). In contrast, the coffee consumption in traditional markets like Europe or the US had an annual average growth rate of 1% in the same period (ICO, 2018).

In this context, coffee and tea together achieved a global market size of \$500bn at the time of the acquisition (Collis & Wert, 2023). Before acquiring Costa, Coca-Cola held a modest share of the \$85bn RTD market. However, Coca-Cola was not part of the \$125bn not-ready-to-drink (NRTD) market, which includes coffee products that require preparation such as coffee beans (Collis & Wert, 2023, Statista, n.d.-a.). Also, the \$360bn out-of-home (OOH) market, which refers to sales of coffee through hotels, restaurants, and other venues, remained untapped by Coca-Cola until then (Collis & Wert, 2023, Mordor Intelligence, n.d.).

Costa faced fierce competition as the coffee market's rapid growth drew major players like Starbucks, Nestlé, and the investment group JAB Holdings, which owns coffee brands such as JDE Peet's and Keurig Dr. Pepper (Gray & Fontanelle-Khan, 2018; JAB Holding, n.d.). While the coffee market remained highly fragmented, these more prominent players strived for consolidation through acquisitions. In the six years leading up to 2018, a total of \$250bn was spent on coffee-related acquisitions (Ahmed et al., 2018; The Guardian, 2018).

Given the intense competition in the coffee market, Costa faced significant pressure from rivals in the coffee house segment (Appendix H). Rivals included the global coffee house chain Starbucks, regional brands such as Luckin Coffee in China (FT Confidential Research, 2018) and the emerging artisan coffee shops (Butler, 2017). By 2018, Starbucks had operated over 29,000 stores worldwide (Statista, 2024) and pursued an aggressive international expansion strategy, opening one store per day in China (Zakkour, 2017).

The competition was fierce, especially in China. Starbucks had 3,000 more stores than Costa in 2018 and aimed to reach 6,000 by 2022 (compared to Costa's 1,200-store target) (FT Confidential Research, 2018). Meanwhile, the Chinese coffee company Luckin Coffee aggressively expanded with discount offerings and a highly technology-driven approach (Shane, 2019). Luckin Coffee, operating 525 stores, had quickly outpaced Costa's footprint in China in 2018 (FT Confidential Research, 2018).

Costa also faced rising competition in its home market, the UK. While it remained the leading coffee house chain, artisan cafés were gaining popularity (Butler, 2017). These cafés attracted customers seeking unique and trendier coffee experiences. Nestlé's \$700m acquisition of Blue Bottle Coffee, an artisanal chain, in 2017 highlighted the increasing importance of artisan competitors (Massoudi et al., 2017).

Competition in the coffee market has affected not only the OOH segment but also the RTD and NRTD segments. PepsiCo, for example, has a longstanding partnership with Starbucks. This partnership captured 97% of the RTD coffee market share in the US and Latin America in 2016 (BevNet, 2015). Meanwhile, Nestlé, the company that dominates the global coffee market, has invested \$7.15bn into Starbucks to secure rights to Starbucks' packaged coffee products, excluding RTD products (Daneshkhu & Atkins, 2018).

4.8 Coca-Cola's Strategic Vision for Costa

While Costa's revenue primarily came from its physical stores and vending machines (Whitbread, 2018), Coca-Cola saw the potential to expand Costa's offering beyond these channels. Coca-Cola's CEO James Quincey emphasized: "Costa is a strong scalable coffee platform which can engage with consumers across multiple channels." (Fleming, 2018, para.9). This strategy also included introducing RTD products (Collis & Wert, 2023; Montgomery & Weber, 2021).

Coca-Cola also intended to boost the revenues made with on-the-go consumption by doubling Costa's vending machines from roughly 10,000 to 20,000 by 2020 and launching the machines in the US market (Montgomery & Weber, 2021). To achieve this, Coca-Cola planned to leverage its operational strength to supply the machines (Montgomery & Weber, 2021). In addition to operational strength, Coca-Cola aimed to utilize its marketing power and global reach to drive Costa's international expansion. James Quincey stated: "Our system can create opportunities to grow the Costa brand worldwide." (Coca-Cola, 2018b, para. 6).

Instead of fully integrating Costa, Quincey aimed to connect Costa to Coca-Cola by retaining Costa's management and brand, for example (Fleming, 2018). Drawing on his experience of previous acquisitions, Quincey explained:

At times we have bought things and tried to make them fit and have not done justice to their category. So first things first we need to see how we win in the coffee market. (Fleming, 2018, para. 2)

4.9 Navigating the Post-Acquisition Journey: Coca-Cola and Costa's Path to Growth

After Coca-Cola received approval for the acquisition from market authorities (World Coffee Portal, 2018), it completed the transaction in January 2019 (Arthur, 2019). Following the completion, Costa was embedded into Coca-Cola's newly established global ventures business unit (Gelski, 2018; Montgomery & Weber, 2021).

The global ventures unit was designed to operate independently from Coca-Cola's geographic structure, maximize the potential of Coca-Cola's acquisitions, and scale brands (Fleming, 2018; Montgomery & Weber, 2021). Unlike regional divisions, the brands from the global ventures unit were not tied to regional targets, allowing them a more flexible and growth-oriented approach (Montgomery & Weber, 2021). Jennifer Mann, who led the business unit at the time, explained this strategy: "Global ventures takes smaller businesses with potential, focuses on them, nurtures them, and works to accelerate their growth without having them overwhelmed by the larger company." (Montgomery & Weber, 2021, p.12). As for Costa, Mann adds: "We are looking to combine the great coffee knowledge at Costa with our marketing expertise, global scale and distribution credentials." (World Coffee Portal, 2019, para. 18).

Dominic Paul, then Costa CEO, appreciated Coca-Cola's approach:

Coca-Cola has been very respectful of our brand and our heritage. Our operating model means that we're connected to Coca-Cola, but not integrated within it. That's important because we can benefit from Coca-Cola's support, while continuing to operate as the Costa Coffee brand that customers know and love. (World Coffee Portal, 2019, para. 11)

Since its acquisition by Coca-Cola, Costa has gone through a period of ups and downs. In 2019, the company reported revenues of £1.3bn (\$1.75bn) (World Coffee Portal, 2024a). However, the outbreak of Coronavirus disease 2019 (COVID-19) hit Costa hard, as James Quincey described it: "It was very much in the crosshairs of the [COVID-19] impact, particularly in 2020 at the beginning when the lockdowns were very severe, and in fact, most of those coffee shops are all closed in 2020, so it was very hard on the Costa business." (Arthur, 2022).

In response to the pandemic's impact, Costa restructured its workforce and cut approximately 1,600 jobs (Butler & Partington, 2020). Despite these measures, Costa reported a loss of £38m (\$46.6m) in 2021 (World Coffee Portal, 2023b).

The years following the pandemic's restrictions were characterized by revenue growth. Costa achieved a 21% increase in revenues, reaching £1.1bn (\$1.36bn) in 2022 (World Coffee Portal, 2023b). This momentum continued in 2023, with revenues rising a further 9% in 2023 to £1.2bn (\$1.6bn), but still remaining below pre-COVID-19 levels (World Coffee Portal, 2024a). While revenue growth resumed, profitability remained a challenge for Costa. After recording a profit of £243m (\$297m) in 2022 (World Coffee Portal, 2023b), the company made a pre-tax loss of £9.6m (\$12.5m) in 2023 (World Coffee Portal, 2024a). This decline was primarily driven by rising costs, particularly in energy and personnel, as well as impairment charges (World Coffee Portal, 2024a).

A key element of Costa's growth strategy has been its international expansion. In 2020, the company made its first move into the US market by acquiring Briggo, a US-based automated coffee machine company (World Coffee Portal, 2020). Two years later, Costa expanded its footprint in the US by opening its first brick-and-mortar stores and launching RTD products (World Coffee Portal, 2022a). Beyond the US, Costa has also been pursuing expansion in other markets. At the end of 2022, Costa announced plans to enter more countries, such as Morocco and Georgia, highlighting its focus on global growth (World Coffee Portal, 2023d).

Costa operated more than 4,000 stores in over 45 markets in October 2024 (World Coffee Portal, 2024a). Among the international markets, India became a key market for Costa's expansion, as Costa's current CEO Philippe Schaillee emphasized: "India is among the top ten priority markets for us." (World Coffee Portal, 2023d, para. 4). By early 2023, Costa had opened its 100th store in India (ANI, 2023) and set an ambitious target of 40-50 new store openings per year (World Coffee Portal, 2023d). In China, however, Costa's progress has been slower than expected and fell short of its initial store target. By 2023, Costa operated approximately 440 stores in China (World Coffee Portal, 2023c).

Beyond its international expansion, Costa continued to grow by exploring new ways to reach customers. The focus of this strategy has been to strengthen its position in the on-the-go coffee market. To achieve this, Costa increased its investments into drive-through stores, as these

stores gained popularity among customers. The company aimed to raise the number of UK drive-through stores from 300 in 2022 to 500 by 2025 (World Coffee Portal, 2022b). Recognizing the potential of this strategy, Costa has also introduced drive-through stores in international markets (World Coffee Portal, 2023a).

To further expand its reach, the company has pursued various partnerships. In 2022, Costa partnered with Freemans Event Partners to provide branded coffee kiosks at major events (World Coffee Portal, 2022d). By 2024, Costa also had secured a partnership with easyJet to offer its coffee on all easyJet flights (World Coffee Portal, 2024d). Other initiatives to extend Costa's reach included partnerships with the supermarket company Sainsbury's to open Costa shops in Sainsbury's supermarkets (World Coffee Portal, 2024b) and with the American hospitality company Delaware North to launch a robotic coffee kiosk concept (World Coffee Portal, 2024c).

In addition to partnerships, Costa has invested in expanding its product portfolio. In June 2019, six months after its acquisition by Coca-Cola, the company first launched RTD products in the UK. Since then, Costa has rolled out RTD offerings in other countries such as China and Poland (Coca-Cola, 2019). Costa targeted primarily younger customers with its RTD products (Arthur, 2023) and quickly gained traction in the market. Costa's RTD division almost doubled in size for the second consecutive year in 2022 (World Coffee Portal, 2022c) and received positive feedback from the customers, as a Costa spokesperson explained: "Response to Costa RTDs has been particularly strong in China and Japan, and we consistently receive positive consumer feedback about the taste of our products." (Arthur, 2023, para. 10).

Beyond RTD products, Costa expanded its self-service segment. In addition to acquiring Briggo, the company collaborated with Delaware North to develop the global-first coffee machine capable of preparing hot and cold coffee beverages (World Coffee Portal, 2024c). Costa's self-service segment grew by 1,500 machines in 2022 alone and operated around 15,000 machines in 20 international markets. Consequently, the self-service segment generated a revenue growth of 5%, resulting in revenues of £348m (\$424m) in 2022 (World Coffee Portal, 2023e).

Costa's new parent company Coca-Cola faced challenges during the pandemic as well. As many restaurants, bars, and entertainment venues closed, the demand for CSD decreased, leading to a drop in Coca-Cola's revenues in 2020 (Rocco, 2021a). However, as social life began

to return, Coca-Cola achieved organic revenue growth of 16% in both 2021 and 2022 (Coca-Cola, 2022). This growth led to an increase in revenue from \$33bn in 2020 to \$43bn in 2022 (Coca-Cola, 2022),

Coca-Cola highlighted Costa's substantial contribution to its 2022 revenue growth and the overall growth of its coffee segment of 13% (Coca-Cola, 2023). In addition to organic growth, Coca-Cola continued to grow beyond its core products through acquisitions. In 2021, the Atlanta-based company acquired the sports drink brand BodyArmor for \$5.6bn, further diversifying its portfolio (Rocco, 2021b). In November 2024, Coca-Cola announced integrating Costa into the reporting lines of its European operating unit (Coca-Cola, 2024). This integration aimed to streamline structures without laying off employees (Coca-Cola, 2024). Moreover, Costa will continue to operate as a stand-alone business (Coca-Cola, 2024).

Coca-Cola's acquisition of Costa was a significant investment in becoming a "total beverage company." The acquisition provided Coca-Cola access to the growing coffee market while introducing challenges in operating a retail business. It will be interesting to see how the two companies will position themselves strategically in the future. Will Coca-Cola and Costa make further acquisitions to expand their offerings in the coffee sector? Moreover, given Costa's struggles, was this acquisition indeed a success for Coca-Cola?

5. Teaching Notes

5.

5.1 Synopsis

The case examines how external developments led to strategic changes within Coca-Cola and the decision to enter the coffee sector. The objective is to present a comprehensive and balanced view of the acquisition, enabling the readers to critically assess the impact of Coca-Cola's entry into the coffee sector.

The case begins by introducing the acquisition and its key protagonists and outlines Coca-Cola's development before the acquisition. In the following sequence, the case illustrates Coca-Cola's changing external environment, such as rising health concerns about its products. This is followed by a description about the transformation towards a "total beverage company" within Coca-Cola under James Quincey's leadership. This transformation included a modernized corporate culture and more agile structures.

Next, Costa's recent performance and the reasons for its sale are outlined. Moreover, to show the potential of the acquisition, the case provides an overview of the coffee market and Coca-Cola's strategic considerations for the acquisition. Finally, the case shows how both companies have developed since the acquisition.

5.2 Teaching Objectives

The case is designed for undergraduate and graduate management students and is particularly suitable for courses related to corporate strategy and acquisitions. It aims to develop a comprehensive understanding of how companies adapt to their business environment, the strategic options available for growth, and how companies efficiently leverage inorganic growth.

The case outlines macro-environmental trends to enhance students' ability to identify and analyze environmental influences on a company. This should help students to develop the capabilities to adapt to market challenges when making strategic decisions.

Another objective is to familiarize students with different growth strategies. By applying the Ansoff Matrix to a real-world scenario, students deepen their understanding of growth strategies and their practical implications.

Furthermore, the case is framed to explore inorganic growth by analyzing Coca-Cola's acquisition motives, assessing the benefits of strategic alliances and acquisitions, and analyzing Coca-Cola's integration measures.

To conclude, the case links theoretical frameworks to a practical case while stimulating critical thinking about the strategic and market dynamics that drove this acquisition.

5.3 Pedagogical Overview

To thoroughly discuss this teaching case, it is recommended that students and teachers prepare themselves, i.e., studying theoretical literature before class. Firstly, it is recommended that readers of the case familiarize themselves with the PESTEL framework to analyze the macro-environmental challenges. Additionally, understanding growth strategies outlined in the Ansoff Matrix is beneficial. Moreover, it is advised that readers have fundamental knowledge of inorganic growth approaches and their motives.

An in-depth understanding of the CSD or the coffee industry is not required before class, as the case provides relevant information about both industries. However, the students and the lecturers should have a broad understanding of how Coca-Cola and Costa operate to assess potential benefits and risks of the acquisition.

5.4 Case Analysis

The assignment questions are discussed below. The answers described here are to be seen as possible solutions. Alternative solutions are possible as long as they are logical and well-reasoned.

Question 1: Examine the macro-environmental factors that impacted Coca-Cola's acquisition of Costa using the PESTEL framework. For each dimension of PESTEL, identify whether relevant factors are present in the case. If so, classify them as either opportunities or threats for Coca-Cola and provide a brief explanation.

Solution: The case does not present technological or environmental trends, and no opportunities are identified in the political, economic and legal dimensions (Table 1).

	Opportunities	Threats
Political	<ul style="list-style-type: none"> ▪ No relevant factors observed 	<ul style="list-style-type: none"> ▪ Political pressure to regulate high-sugar beverages
Economic	<ul style="list-style-type: none"> ▪ No relevant factors observed 	<ul style="list-style-type: none"> ▪ Rising costs in coffee industry due to increased wages and bean prices
Social-cultural	<ul style="list-style-type: none"> ▪ Coffee consumption increased worldwide 60% in two decades (especially in emerging countries strong increase) 	<ul style="list-style-type: none"> ▪ Growing health concerns over obesity ▪ Shift from CSD to coffee for caffeine ▪ Demand for unique CSD flavors ▪ CSD industry was criticized for not doing enough to address health issues
Technological	<ul style="list-style-type: none"> ▪ No relevant factors observed 	<ul style="list-style-type: none"> ▪ No relevant factors observed
Environmental	<ul style="list-style-type: none"> ▪ No relevant factors observed 	<ul style="list-style-type: none"> ▪ No relevant factors observed
Legal	<ul style="list-style-type: none"> ▪ No relevant factors observed 	<ul style="list-style-type: none"> ▪ Sugar taxes in multiple countries and US regions

Table 1: PESTEL Analysis

Political - Threats

Governments across Europe and the US observed the CSD industry more closely regarding the negative impact of its beverages on people’s health. As a result, Coca-Cola had to fear further political restrictions.

Economic – Threats

An economic factor to consider in the acquisition was the rising costs in the coffee industry. Increasing bean prices and barista wages primarily drove these costs. This was relevant for Coca-Cola, as it needed to be aware of the environment of its acquisition target.

Social – Opportunities

Global coffee consumption has increased by 60% in the last two decades, showing a shift in consumer preferences. Coffee has become increasingly popular, especially in emerging countries. Therefore, this has created an opportunity for Coca-Cola to capitalize on the growing coffee consumption.

Social – Threats

As coffee grew in popularity, CSD consumption decreased in Western markets. This was due to health concerns as the obesity rate nearly doubled worldwide in 40 years. As a result, consumers turned away from sugary beverages and increasingly substituted CSD with coffee as their primary source of caffeine. Those who still drank CSD looked for more unique flavors, increasing the pressure on Coca-Cola to expand its product portfolio. Additionally, the CSD industry faced criticism from the media for not doing enough to prevent health issues linked to its products. As a result, Coca-Cola and the entire industry were under pressure to maintain their reputation.

Legal – Threats

The introduction of sugar taxes in European countries and parts of the US put legal pressure on Coca-Cola. This has been observed in Philadelphia, for example, where the sugar tax had a direct negative impact on CSD sales.

Question 2: Analyze Coca-Cola's acquisition of Costa by examining the four acquisition motives: value creation, managerial self-interest, environmental factors, and firm characteristics. Identify how each motive is present in the case, describe its impact on the acquisition decision, and determine which motives were the primary drivers behind the transaction.

Solution: The acquisition was primarily driven by value creation, environmental factors, and firm characteristics while managerial self-interest is less prominent.

Value Creation

A key motive behind Coca-Cola's acquisition of Costa was value creation, as the acquisition allowed Coca-Cola to increase its market power in the coffee market. Although it already had a presence in the coffee market through Georgia Coffee, its role in the global coffee market was negligible. By acquiring a global player such as Costa, Coca-Cola immediately gained relevance in the global coffee market and had the power to compete with other global players. In addition, the acquisition offered Coca-Cola the opportunity to use its strengths to create synergies with Costa. For example, Coca-Cola could leverage its global distribution network and marketing expertise to promote Costa's product.

Environmental Factors

In addition, environmental factors played a key role in this acquisition. Customers' health concerns, regulatory restrictions, and the negative media perception of CSD companies have challenged Coca-Cola's traditional business model. Through its entry into the coffee market, Coca-Cola mitigated these risks by offering a product category with a healthier consumer perception and further reducing its dependence on its CSD business.

Additionally, industry trends and competitive dynamics influenced Coca-Cola's decision. The global coffee market was gaining relevance as consumption increased. Hence, the coffee industry presented an attractive investment opportunity for Coca-Cola. Furthermore, the sociological aspect was prevalent, as Coca-Cola's rival PepsiCo had already invested in the coffee market through its Starbucks partnership. Therefore, Coca-Cola may have felt inclined to imitate this not to miss the opportunity in the coffee market, and fall behind its competitors.

Firm Characteristics

Firm characteristics, such as acquisition experience, were critical in this acquisition. Before the acquisition of Costa, Coca-Cola had gained acquisition experience through various acquisitions, such as Innocent. This has likely supported Coca-Cola's confidence in pursuing transactions. Furthermore, establishing the global ventures unit to foster acquisitions facilitated the acquisition. Another firm-specific factor was Coca-Cola's strategic positioning of becoming a "total beverage company." Expanding its product portfolio through acquisitions was vital for reaching this goal, as James Quincey considered acquisitions an important part of Coca-Cola's strategy.

Managerial Self-Interest

There was limited evidence that managerial self-interest was decisive in this acquisition. The high multiple that Coca-Cola has paid may indicate overconfident managers and managerial self-interest. However, the acquisition appeared rational and strategically motivated as it aligned with Coca-Cola's overarching strategy rather than being motivated by an empire-build-

ing vision from James Quincey. In this case, other factors, such as value creation and environmental factors, appeared more pressing than potential managerial self-interest.

Question 3a: Critically discuss the acquisition of Costa by examining the potential benefits and risks of the acquisition for Coca-Cola.

Solution: The acquisition had several benefits for Coca-Cola, the main ones being: immediate market expansion, cross-selling, operational synergies, and financial risk mitigation.

First, a benefit was that Coca-Cola did not have to build a global coffee brand from the ground up, which would have required more time. Instead, Coca-Cola could immediately leverage Costa's brand and infrastructure. Additionally, the acquisition gave Coca-Cola complete control over its expansion into the coffee sector, rather than relying on a partner.

Furthermore, Costa, the world's second largest coffee house chain, offered Coca-Cola a large existing customer base. This allowed Coca-Cola to cross-sell its CSD products in Costa's coffee shops and vending machines. At the same time, Costa's RTD products could be integrated into Coca-Cola's existing vending machines to sell coffee products to Coca-Cola's customers.

Another potential benefit arose from operational synergies. Coca-Cola could use its supply chain to supply Costa's vending machines with products and its marketing expertise to promote Costa. Additionally, Coca-Cola's strong global presence could help Costa expand internationally. Moreover, Coca-Cola's expertise in RTD products, a previously untapped segment by Costa, offered potential to drive Costa's growth.

Finally, Coca-Cola diversified its revenue streams through this acquisition. As Coca-Cola was highly dependent on CSD sales, it was vulnerable to changes in the CSD environment. Therefore, this acquisition increased its resilience to environmental changes by broadening the product portfolio. Moreover, Costa's strong customer base, with over 5m enrolled in its loyalty program, ensured stable revenues.

However, the acquisition posed several risks, including financial risks, Costa's mixed performance before the acquisition, operational challenges, and the integration of Costa.

The acquisition was a significant financial commitment. Paying a price that was valued higher than Starbucks' multiple pressured Coca-Cola to generate strong returns from this investment, which has not been achieved until now.

Additionally, Costa had not shown strong sales growth in the years before the acquisition. It faced rising costs and struggled to grow organically, indicated by the stagnating like-for-like sales. Although Costa was the leading coffee house chain in the UK, it faced difficulties expanding internationally before the acquisition. It did not have a presence in the US. Moreover, it experienced challenges in China, one of its key international markets, with Starbucks dominating the Chinese coffee house market and Luckin Coffee outpacing Costa. All these factors raised questions about whether Costa will be able to grow in the future.

In addition, Costa's operational model challenged Coca-Cola. While Coca-Cola had strengths in RTD products, it had no experience managing a global retail chain. Therefore, the differences between the two companies' operating models could limit the potential synergies.

Finally, the integration of Costa into Coca-Cola posed risks in terms of culture and organizational structure as the acquisition increased Coca-Cola's headcount by approximately 20,000 employees. These employees were all familiar with Costa's processes and culture but had to be integrated into the Coca-Cola conglomerate.

Question 3b: Briefly analyze which strategy (preservation, symbiosis, absorption, intensive care, reorientation) Coca-Cola pursued to integrate Costa.

Solution: Coca-Cola pursued a reorientation strategy to integrate Costa. This strategy allowed for a balance between autonomy retention and knowledge transfer.

Retention of Autonomy

Coca-Cola emphasized that it did not intend to fully absorb Costa's identity or assets. Instead, it linked Costa to Coca-Cola's organization by creating the global ventures unit and keeping Costa as a standalone brand. The global ventures unit enabled Costa to operate more independently from regional targets. Dominic Paul, Costa's CEO at the time, confirmed that Costa retained its culture and processes. Furthermore, after Costa was integrated into the Coca-Cola reporting system, it continued to operate as a stand-alone business, emphasizing its autonomy.

This rules out an absorption or intensive care strategy. Both of these approaches would have required a more drastic restructuring of Costa.

Knowledge Transfer

At the same time, there was a knowledge transfer to some extent. Jennifer Mann, then leader of the global ventures unit, highlighted that Coca-Cola would support Costa in marketing, for example. Also, the announced integration of Costa into Coca-Cola's Europe reporting system indicates the knowledge transfer between these companies, as it probably requires closer collaboration between their finance and reporting teams.

Therefore, the knowledge transfer between the two companies was too substantial to be classified under a preservation strategy, as this involves minimal integration. At the same time, the knowledge transfer between the companies was not comprehensive enough to classify the integration as a symbiosis since the knowledge transfer concerned only very selected functions, such as marketing and reporting.

Question 4: Imagine Coca-Cola had the opportunity to form a strategic alliance with Costa instead of acquiring it. Would this have been a better approach for its entry into the coffee market? Analyze the advantages and disadvantages that Coca-Cola would have had by pursuing a strategic alliance compared to the acquisition, and justify whether the acquisition was the right decision.

Solution: A strategic alliance would have offered several advantages, including lower financial risk, a more explicit focus on each company's core strengths, and greater flexibility for Coca-Cola.

First, a strategic alliance would have required a lower financial investment from Coca-Cola. While Coca-Cola would still need to invest in a strategic alliance, the investment would presumably have been less than the \$5.1bn acquisition price. Therefore, a strategic alliance would have involved less financial risk for Coca-Cola, providing an opportunity for a low-cost entry into the coffee market.

Second, an alliance would have allowed Coca-Cola and Costa to focus more on their respective specializations. Coca-Cola could have concentrated on RTD and vending machines, which

would have aligned with its existing business. At the same time, Costa could have focused on coffee production and retail operations. As a result, Coca-Cola would not have had to learn how to run a retail-heavy business but could have leveraged more of its existing strengths. At the same time, a strategic alliance would have enabled Coca-Cola to build up its knowledge about retail stores and the coffee industry, so that it would eventually have the required expertise to launch a coffee chain itself.

Lastly, a strategic alliance would have given Coca-Cola greater flexibility. Due to the lower financial investment, it would have been possible to treat the alliance as a pilot project for entering the coffee market. Coca-Cola could have left the alliance relatively quickly or adapted its approach, avoiding the long-term commitment of an acquisition.

At the same time, pursuing a strategic alliance would have presented Coca-Cola with several disadvantages, such as less control, less growth potential, and the loss of knowledge.

Firstly, Coca-Cola would have depended on its partner in a strategic alliance, resulting in less control over its expansion strategy. While the alliance would allow Coca-Cola to enter the coffee market, Coca-Cola would have relied on Costa's direction and decisions.

Secondly, because a strategic alliance would involve a shared financial investment by both alliance partners, it would also diminish Coca-Cola's long-term growth potential, as it would always have to share the profits with its partner.

Lastly, a strategic alliance could have led to a loss of knowledge. For example, by sharing Coca-Cola's expertise in marketing, Costa could use the gained know-how and thereby become independent of a strategic alliance with Coca-Cola.

Given that Coca-Cola was not a relevant player in the coffee market, the company was in danger of missing a significant opportunity, and an aggressive strategic move was needed. The acquisition of Costa immediately gave Coca-Cola an extensive store network and opportunities to achieve synergies, for example through cross-selling opportunities. This could not have been achieved to a comparable extent through a strategic alliance, leading to the conclusion that the acquisition was the better decision.

Question 5a: Classify Coca-Cola's acquisition of Costa within the Ansoff Matrix and justify your classification.

Solution: Based on the Ansoff Matrix, Coca-Cola's acquisition of Costa can be considered a diversification strategy as Coca-Cola enters new markets with new products.

Product

The acquisition was Coca-Cola's first entry into the hot beverage market, which differed from the CSD market regarding products. While Coca-Cola already owned Georgia Coffee and produced RTD coffee, it could be argued that selling hot coffee was only a minor product modification. However, given the significant differences in operations and skills required for RTD coffee and coffee served in a coffee shop, this acquisition appeared to involve new products. In addition, Costa sold coffee as well as food, a product that Coca-Cola had not sold before. Although food was not Costa's core product, it adds to the argument of new product involvement.

Market

The acquisition allowed Coca-Cola to enter the OOH coffee market, whereas Coca-Cola had only been a small part of the RTD coffee market. Compared to its CSD and RTD coffee customers, Coca-Cola gained new customer segments, such as urban consumers who enjoy a convenient coffee shop experience. Consequently, Coca-Cola expanded into a new market through this acquisition.

Question 5b: Analyze Costa's growth initiatives after its acquisition by Coca-Cola using the Ansoff Matrix. Briefly classify Costa's expansion efforts within the four strategic growth categories, and outline the opportunities for Costa associated with each approach.

Solution: Costa's growth strategy after the acquisition is an adequate example of a company not following a single growth strategy but pursuing several paths simultaneously.

Market Penetration

Costa implemented a market penetration strategy by aiming to increase sales in its existing UK market through its current product, hot coffee. A key element was the expansion of drive-through stores. This enhanced Costa's reach and appealed to customers seeking more conve-

nience. Strategic partnerships, like those with Freeman Event Partners and Sainsbury's, made Costa's products more accessible and mitigated its dependence on its stores in shopping centers. Through the market penetration initiatives, Costa has diversified its distribution channels, further integrated the brand into the daily lives of its customers and increased brand awareness.

Market Development

Costa pursued a market development strategy by expanding into new geographic regions with existing products. Key steps included entering the US market by acquiring Briggo, a product similar to its existing vending machines, and the US launch of brick-and-mortar stores. The entry into the US provided access to a large market with great sales potential. Moreover, Costa's expansion into emerging markets like India has allowed the company to benefit from rising coffee consumption in emerging markets. The expansion into emerging markets gave Costa an early-mover advantage and the opportunity to establish a strong brand loyalty before competition intensified.

Product Development

Costa's collaboration with Delaware North to develop a machine for hot and cold coffee beverages is a product development initiative. The machine represents a technological advancement rather than a minor product modification since it is the world's first machine capable of preparing hot and cold coffee beverages. This initiative expands Costa's customer base in the coffee machine segment by attracting customers looking for cold coffee and provides a technological lead over its competitors.

Diversification

Costa's introduction of RTD products marked a shift from its retail business to packaged beverages. While it was still coffee, the RTD products required different processes and skills. Additionally, the launch of the RTD products allowed Costa to enter the RTD market, which was previously untapped by the company. Therefore, as Costa introduced a new product to a new market, this initiative is classified as a diversification. This move provided Costa with a new revenue stream in a fast-growing category while creating synergies through Coca-Cola's distribution capabilities and expertise in the RTD segment.

Recognizing that there are more initiatives mentioned in the case, further topics could be discussed.

5.5 Teaching Approach

The case is designed for a 90-minute class (Table 2). Before the class, each student should have read the case and prepared answers to each question. The teacher then divides the class into five groups and assigns one question to each group. Each group should discuss its results within the group. Finally, each group presents the results of the assigned task in an upfront presentation. A discussion with the rest of the class follows each presentation. This cooperative learning approach aims to develop students' business and interpersonal skills, such as considering different perspectives and resolving conflicts (Gillies, 2003). The oral classroom presentation approach aims to improve students' communication skills (Girard et al., 2011), as effective communication is essential for future professional careers (Majid et al., 2012).

Content	Time (in minutes)
Brief Introduction & Assigning Students into Groups	10
Discussion within each Group	15
Presentation & Discussion of Question 1: Macro-Environmental Factors	10
Presentation & Discussion of Question 2: Acquisition Motives	10
Presentation & Discussion of Question 3: Acquisition Risks & Gains	15
Presentation & Discussion of Question 4: Strategic Alliance	10
Presentation & Discussion of Question 5: Growth Strategies	15
Conclusion	5

Table 2: Timetable for a 90-Minute Class

6. Limitations

Although this case provides a comprehensive view of the acquisition, it is subject to certain limitations.

Firstly, a limitation of this thesis is its temporal focus. The case focuses on the years immediately before and after the acquisition. As a result, the analysis may overlook long-term strategic developments within each company that may have influenced the acquisition decision. In addition, due to the recency of the acquisition, the long-term success of the acquisition remains to be seen.

Secondly, the pandemic poses another limitation as it has affected the post-acquisition development. Consequently, the impact of COVID-19 makes it difficult to compare the acquisition with acquisitions made by Coca-Cola before COVID-19.

Thirdly, not all macro- and micro-environmental trends can be captured. Although the case provided insights into important trends within the companies' business environment, it is not possible to consider every event.

Finally, this case is based on publicly available data. Therefore, a lack of internal information may have limited the depth of the study since internal challenges and considerations may not have been fully described based on publicly available data. In addition, publicly available data may be described overly positively by the companies, which may have caused a bias in the case description.

7. Conclusion

This thesis explored how companies leverage growth strategies and inorganic growth approaches in a demanding business environment. Since achieving corporate growth in the consumer goods sector is particularly challenging, this thesis examined the example of Coca-Cola's acquisition of Costa as part of its mission to become a "total beverage company."

Compared to existing cases on Coca-Cola, this case is the first to illustrate macro-environmental developments in depth, both within Coca-Cola's current environment and in the coffee market that the company is entering. By outlining opportunities such as the growing global coffee consumption and risks like the increasing taxes on sugary beverages, the case provides a more balanced view of this acquisition.

In addition, the case includes a detailed description of the companies' performance before the acquisition. Incorporating Costa's recent developments, such as its stagnating like-for-like sales, allows the reader to critically analyze the potential and risks of this acquisition.

Moreover, this case explores Costa's post-acquisition development more thoroughly than existing cases by outlining Costa's various partnerships, for example. This enables the reader to understand the complexity of various growth strategies. Furthermore, due to the richness of the data in this case, it has the potential to be explored through other theoretical lenses, such as internationalization, making it a valuable asset in many teaching classes.

However, the case has limitations, such as its focus on a specific period. Therefore, future research could address this by conducting a longitudinal study of this acquisition to analyze how the synergies have evolved in the long term. Furthermore, it would be interesting to compare this acquisition with other acquisitions made during the pandemic to understand how Coca-Cola's acquisition performed compared to other acquisitions.

In conclusion, this thesis provides insights into business environments, corporate growth strategies, and inorganic growth. It highlights the opportunities for achieving growth through acquisitions, such as immediate market access, and complexities, like integrating the acquired company.

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Appendix

Appendix A: Coca-Cola Income Statement 2018 (Coca-Cola, 2018a)

Year Ended December 31,	2018	2017	2016
(In millions except per share data)			
NET OPERATING REVENUES	\$ 31,856	\$ 35,410	\$ 41,863
Cost of goods sold	11,770	13,255	16,465
GROSS PROFIT	20,086	22,155	25,398
Selling, general and administrative expenses	10,307	12,654	15,370
Other operating charges	1,079	1,902	1,371
OPERATING INCOME	8,700	7,599	8,657
Interest income	682	677	642
Interest expense	919	841	733
Equity income (loss) — net	1,008	1,071	835
Other income (loss) — net	(1,121)	(1,764)	(1,265)
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	8,350	6,742	8,136
Income taxes from continuing operations	1,623	5,560	1,586
NET INCOME FROM CONTINUING OPERATIONS	6,727	1,182	6,550
Income (loss) from discontinued operations (net of income taxes of \$126, \$47 and \$0, respectively)	(251)	101	—
CONSOLIDATED NET INCOME	6,476	1,283	6,550
Less: Net income attributable to noncontrolling interests	42	35	23
NET INCOME ATTRIBUTABLE TO SHAREOWNERS OF THE COCA-COLA COMPANY	\$ 6,434	\$ 1,248	\$ 6,527
Basic net income per share from continuing operations ¹	\$ 1.58	\$ 0.28	\$ 1.51
Basic net income (loss) per share from discontinued operations ²	(0.07)	0.02	—
BASIC NET INCOME PER SHARE	\$ 1.51	\$ 0.29³	\$ 1.51
Diluted net income per share from continuing operations ¹	\$ 1.57	\$ 0.27	\$ 1.49
Diluted net income (loss) per share from discontinued operations ²	(0.07)	0.02	—
DILUTED NET INCOME PER SHARE	\$ 1.50	\$ 0.29	\$ 1.49
AVERAGE SHARES OUTSTANDING — BASIC	4,259	4,272	4,317
Effect of dilutive securities	40	52	50
AVERAGE SHARES OUTSTANDING — DILUTED	4,299	4,324	4,367

¹ Calculated based on net income from continuing operations less net income from continuing operations attributable to noncontrolling interests.

² Calculated based on net income (loss) from discontinued operations less net income from discontinued operations attributable to noncontrolling interests.

³ Per share amounts do not add due to rounding.

Figure 3: Coca-Cola Income Statement 2018 (Coca-Cola, 2018a)

Note: A refranchising of the bottling business has led to a \$10bn sales decline between 2015 and 2018 (Montgomery & Weber, 2021)

Appendix B: Coca-Cola Sales Volume by Category 2018 (Coca-Cola, 2018a)

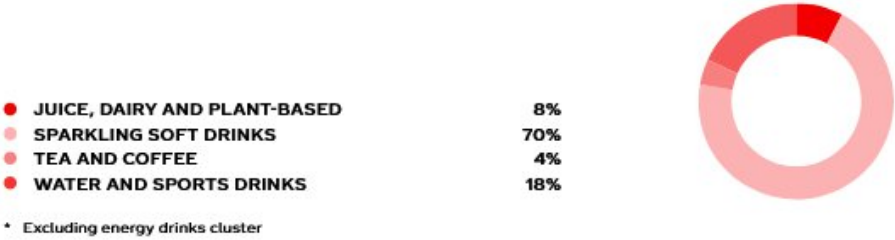


Figure 4: Coca-Cola Sales Volume by Category 2018 (Coca-Cola, 2018a)

Appendix C: Costa's Stores Worldwide in 2018 (Green, 2018)

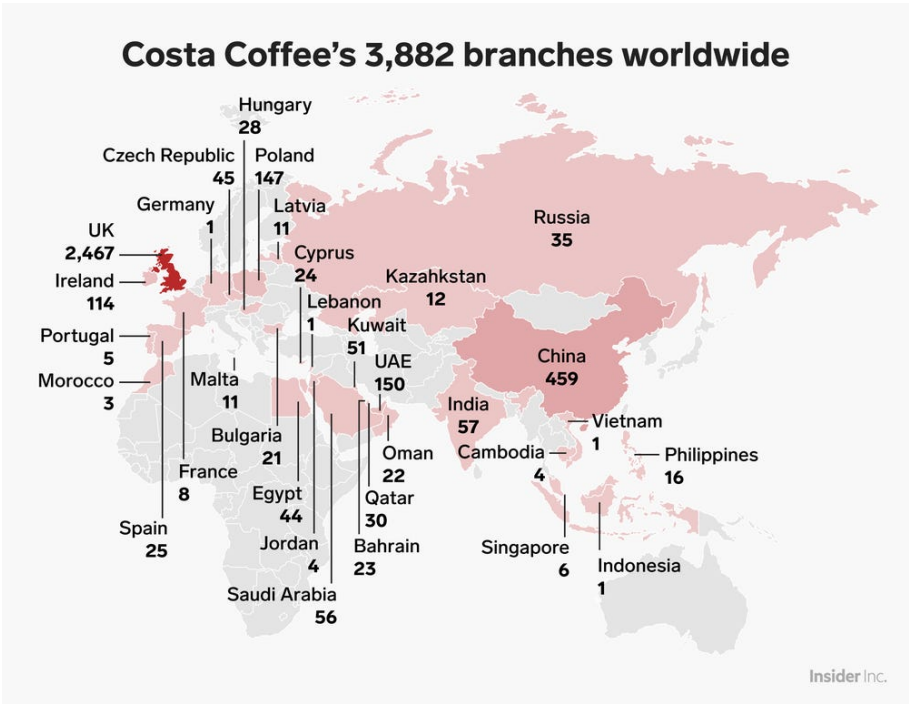


Figure 5: Costa's Stores Worldwide in 2018 (Green, 2018)

Appendix D: Conversion Rates (Macrotrends, n.d.)

Not all sources used in this thesis provided financial figures in US-Dollars (USD) but instead reported values in British Pounds (GBP). The figures were manually converted into USD for the cases highlighted in the text to ensure consistent numbers for the reader.

The conversion was based on the Yearly Average Closing Price of the GBP against the USD for the respective years. The table below presents the relevant exchange rates for these conversions (Table 3).

Year	GBP to USD - Yearly Average Closing Price
1995	1.58
2017	1.29
2018	1.33

Table 3: Conversion Rate GBP to USD (Macrotrends, n.d.)

Appendix E: Costa's Like-for-Like Sales Development (Butler, 2017)

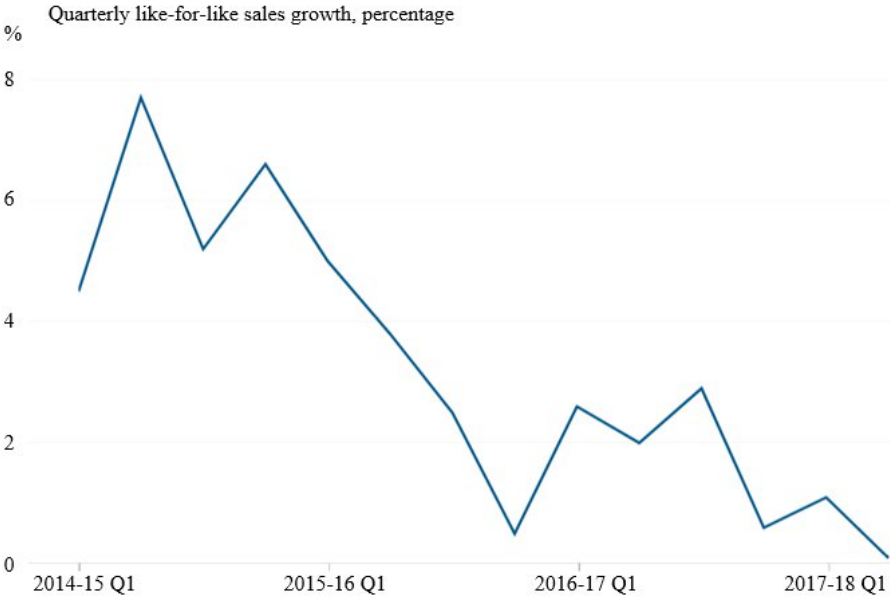


Figure 6: Costa's Like-for-Like Sales Development (Butler, 2017)

Appendix F: World Coffee Consumption (ICO, 2018)

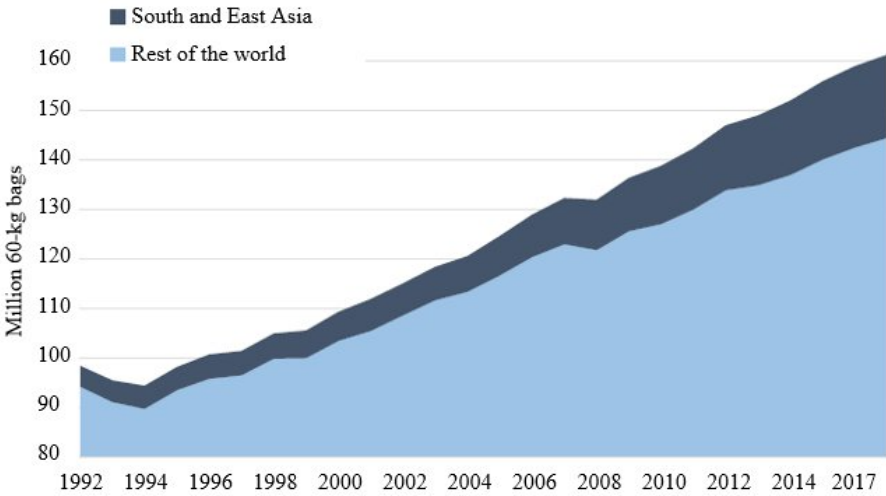


Figure 7: World Coffee Consumption (ICO, 2018)

Appendix G: Coffee Consumption in Asian Countries (ICO, 2018)

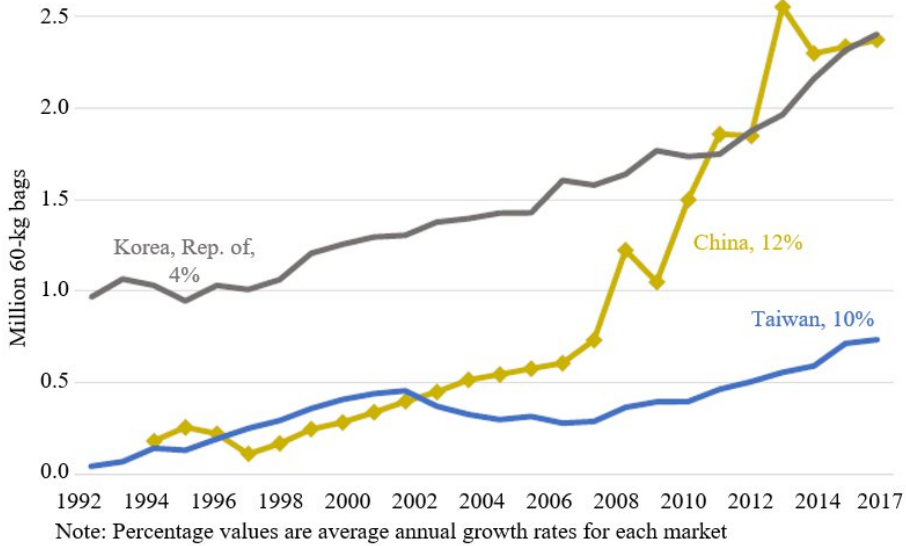


Figure 8: Coffee Consumption in Asian Countries (ICO, 2018)

Appendix H: Coffee Chains by Consumer Brand Preference (%) in China (FT Confidential Research, 2018)

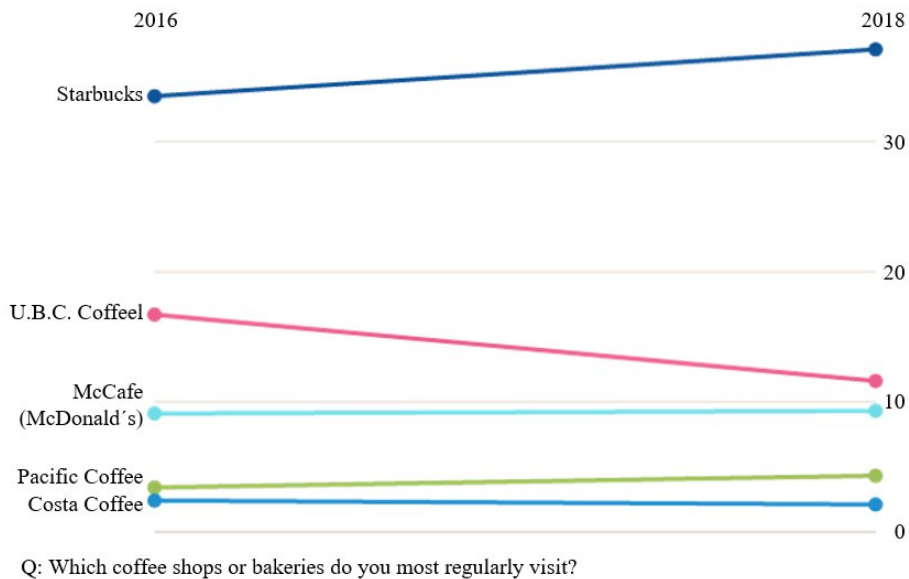


Figure 9: Coffee Chains by Consumer Brand Preference (%) in China (FT Confidential Research, 2018)

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