Finally, Coke Gets It Right in India

By Manjeet Kripalani in Bombay, with Mark L. Clifford (BusinessWeek)
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You might think selling in India would be a romp for beverage giant Coca-Cola Co. The country has a billion-plus consumers, a growing middle class, and the climate is hot, hot, hot. Look a little more closely, though, and this market is more minefield than mother lode. Sure, Coke's various beverages have more than half the market. But its flagship brand--Coca-Cola, the ur-soft drink--remains a distant third, with an estimated market share of 16.5%, far behind arch rival Pepsi-Cola's 23.5%. Almost as embarrassing, No. 2 is Thums Up, a sweeter local cola that Coke acquired in 1993, then proceeded to neglect. "The environment in India is challenging," says Alex von Behr, a Briton who is president of Coke India. "But we're learning how to crack it."

The learning curve has been steep. In 1993--15 years after being thrown out by India's socialist government--Coke stormed back into the country with big plans to wrest control from Pepsi and the local beverage marketers that had risen up in its absence. Instead, the company spent years on the defensive after overestimating the size of the market, misreading consumers, and battling with the government. A semi-farcical tussle in which Coke bottlers hoarded empty Pepsi bottles gave the company a black eye until the dispute was resolved last November. And Coke India has been hurt by a revolving door in the executive suite. In 10 years, it has had five expatriate heads. Pepsi, by contrast, last year appointed its third Indian chief executive in 14 years. The result: In 2000, Coke wrote down the value of its Indian bottling assets by $405 million. It has suffered losses in India for years--although its execs won't reveal financial details.

Finally, Coke is starting to inject some fizz into its Indian operations. On Feb. 28, the company plans to sell 49% of its Indian bottler, Hindustan Coca-Cola Beverages, for $41 million. The sale won't be the domestic stock listing that some in New Delhi had sought. Instead, the shares will be sold in a private placement with institutional investors and employees. But it puts to rest a thorny issue that had chilled relations with the government, which wanted Indians to have a substantial ownership stake in Coke's local operation. Better yet, Indians appear to be developing a taste for Coke products: The company's overall sales in India jumped 24%, to $940 million, last year. "Coke lost a number of years over errors," says Jagdeep Kapoor, chairman of Samsika Marketing Consultants in Bombay. "But at last, it seems to be getting its positioning right."

That will come as a great relief at Coke headquarters in Atlanta. India, with soft-drink consumption of just seven 8-ounce (250 milliliters) servings per capita annually, holds more potential for growth than just about any other market on earth. By contrast, neighboring Pakistan hoists an average of 14 servings per year; in China, it's 89; and in Mexico, the world's hottest soda market, it's nearly 1,500 servings. Determined to consolidate its position and boost growth, Coke this year cut prices on all of its beverages by an aggressive 15% to 25%, forcing Pepsi to follow suit. "India is the beverage battlefield for 2003," says Ronald S. McEachern, Pepsi's Asia chief.

Key to Coke's battle plans is operations chief Sanjeev Gupta. After being promoted from marketing director three years ago, the boyish, straight-talking Gupta persuaded his Coke bosses to change the way they do business. "He bravely stood up to Atlanta and told them their strategy in India was wrong," remembers a former Coke exec in New Delhi. Gupta's first step: revitalizing Thums Up, which led the market in 1993 with more than 60% of carbonated beverage sales but had slipped to just 15% by 1998. After Atlanta gave the green light to pushing local brands as much as Coca-Cola, the 41-year-old Gupta spent $3.5 million to beef up advertising and distribution for Thums Up. Within a year, he built it into India's No. 2 soda.

Then Gupta--a veteran of marketing juggernaut Hindustan Lever Ltd.--persuaded Atlanta to revamp pricing and advertising for Coca-Cola. In 2001, he launched a new size, a 200-ml. bottle that sells for 10 cents and is aimed at rural areas and lower-income urban markets. This year he dropped the price of a 300-ml. bottle to 17 cents from 24 cents. The price cuts were key to boosting sales and the little bottle was a big hit. Gupta expects it to represent 50% of sales by volume this year.

In 2002, after years of lackluster ad campaigns, Gupta's team settled on an advertising strategy that caught the imagination of Indians. Breaking with Coke tradition, he hired a celebrity spokesman, Bollywood movie star Amir Khan. The campaign equates Coke with "thanda," the Hindi word for "cold," a commonly used term for a generic soft drink. "Coke had to break a lot of its rules for India," recalls Ashok Jain, the former head of Cadbury Schweppes PLC in India, who quit Schweppes after Coke bought it in 1999.

The company has been cutting costs, too. Although Coke owns 70% of its bottlers, many of them were outdated operations inherited from the Thums Up purchase. Over the past three years, it has shut down eight of them, which helped trim the payroll by 23%, to 5,000. Employee costs have fallen to 4.5% of revenues from 7% in 2002. Coke got rid of about 80 managers, including high-priced top execs, earning Gupta the moniker "Prince of Darkness." It saved 57% on import duties by using more local raw materials. And by upgrading its bottling technology and improving maintenance and training, Coke has improved plant efficiencies by 40%. Says Gupta: "We were saddled with chaotic operations, but that's all changed."

At the same time, Coke is branching out into other products. In 2001, it introduced Kinley bottled water, which has grown to a leading market share of 37% by building on Coke's distribution network to reach far-flung villages. Key to Kinley's expansion have been ads depicting village life and military families that, given India's constant security concerns, have "built an emotional connect with the Indian consumer," says consultant Kapoor. Encouraged, Coke is now copying the success of its ready-to-drink coffee in Japan and test-marketing the concept in India.

Finally, it has settled its long-standing dispute with Pepsi over bottles. Last November, Pepsi accused Coke of hoarding more than 5 million of its bottles, which had ended up in Coke's hands from recyclers. Without them, Pepsi had difficulty meeting demand for its drinks. On Nov. 26, after Pepsi called the police and a court ordered Coke to return the bottles, the two companies agreed to regular exchanges.

The changes are paying Coke dividends. Execs at Coca-Cola India say the company is no longer losing money. "We have turned a corner," says N. Sridhar, Coke India's finance director. "This will release our energies to concentrate on building market share." Now, Coke is planning on investing $150 million more to expand its bottling and distribution network. That will make India Coke's second-largest Asian investment after China. The subcontinent hasn't become a mother lode for Coke yet. But the company sure is trying to make it one.

Questions

1. Coca-Cola Co. has suffered losses in India for years. Why has Coke invested in a negative NPV project? Why has PepsiCo India been successful?

2. Describe the factors that Coke did not take into consideration in their 1993 study of investing in Coke India. Explain clearly the effect of those factors in the NPV of the project.

3. According to N. Sridhar, Coke "has turned a corner." With the information provided in the article –and making reasonable assumptions-, derive the NPV of Coke India.

4. Coke is planning to invest USD 150 million to expand its bottling and distribution network in India. Describe the exposure to currency risk. Explain how the currency risk may be affected if Coke decides to finance the investment with loans from Indian banks.

5. What factors should Coke consider to derive its required rate of return on the expansion plan for Coke India.